SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1935

No. 525

GREAT WESTERN POWER COMPANY OF CALIFORNIA, PETITIONER,

vs.

COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

INDEX.

	Original	Print
Proceedings before United States Board of Tax Appeals....	1	1
Docket entries	1	1
Petition	5	3
Exhibit "A"—Notice of deficiency.....	13	8
Letters rejecting claims for refund..	27	14
Answer	29	15
First Amended Petition	31	16
Answer to First Amended Petition.....	40	22
Settlement Under Rule 50 (Respondent's)	47	26
Opinion, Van Fossan, M., ...	61	36
Dissenting opinion, Sternhagen, M., ...	77	46
Motion to Amend Opinion.....	78	46
Decision	79	47
Petition for Review and Assignments of Error.....	80	48
Notices of Petition for Review	98	59
Motion to Correct Record	101	60
Order Granting Motion to Correct Record (2d Circuit)..	103	61
Statement of Evidence	104	62
Caption	104	62
Stipulation of Facts	105	63
Stipulation of Facts No. 2	110	66

JUDD & DETWEILER (INC.), PRINTERS, WASHINGTON, D. C., JANUARY 4, 1936.

—7275-C

	Original	Print
Proceedings before United States Board of Tax Appeals.—Continued.		
Exhibit "A"—Refunding mortgage, March 1, 1919	123	74
Exhibit "A-1"—Resolutions of Dec. 7, 1920	133	80
Exhibit "A-2"—Resolutions of April 8, 1921	142	86
Exhibit "A-3"—Resolutions of June 21, 1921	143	87
Exhibit "A-4"—Resolutions of Feb. 5, 1925	144	87
Exhibit "B"—Mortgage indenture, Aug. 1, 1920	155	94
Exhibit "C"—General lien indenture, Feb. 1, 1921	163	99
Exhibit "D"—Resolutions of May 8, 1924	177	107
Exhibit "E"—Opinion and order of Railroad Commission of California, Application No. 11111	179	108
Exhibit "F"—Opinion and order of Railroad Commission of California Application No. 10785	183	111
Exhibit "G"—Opinion and order of Railroad Commission of California, Application No. 11759	190	116
Exhibit "H"—Extract from minutes of special meeting of Board of Directors held on Feb. 5, 1925	196	119
Exhibit "I"—Extract from minutes of special meeting of Board of Directors held May 15, 1925	199	121
Exhibit "J"—Extract from minutes of special meeting of Board of Directors, held Sept. 25, 1925	211	129
Stipulation of facts No. 3	214	131
Order approving statement of evidence	216	132
Præcipe for record	216	132
Clerk's certificate (omitted in printing)		219
Proceedings in U. S. C. C. A., Second Circuit	220	135
Note of issue	220	135
Order on motion to dismiss	221	136
Motion to dismiss	223	136
Order denying motion to dismiss	224	137
Opinion, Chase, J.	226	137
Decree	234	142
Clerk's certificate	236	143
Order allowing certiorari	237	145

[fols. a–c–1]

BEFORE UNITED STATES BOARD OF TAX APPEALS

Docket No. 48617

GREAT WESTERN POWER COMPANY OF CALIFORNIA, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

DOCKET ENTRIES

Appearances:

For Petitioner: Thomas R. Dempsey, Esq.
For Respondent: F. R. Shearer, Esq.

1930.

May 2. Petition received and filed. Taxpayer notified (Fee paid.)

May 3. Copy of petition served on General Counsel.

June 16. Answer filed by General Counsel.

June 18. Copy of answer served on taxpayer—Circuit Calendar.

1933

June 5. Stipulation of facts filed.

July 3. Hearing set for week of Sept. 11, 1933 at San Francisco, Calif.

[fol. 2]

1933.

Sept. 19. Hearing had before Mr. Van Fossan, Division 9, on merits. Amended petition and amended answer filed—copies served. Stipulations of facts #2 and #3 filed. Motion for judgment filed by petitioner—copy served.

Oct. 16. Transcript of hearing Sept. 19, 1933 filed.

1934

Apr. 26. Opinion rendered—Mr. Van Fossan, Division 9. Decision will be entered under Rule 50.

June 6. Motion to amend opinion filed by taxpayer. 6/12/34 granted (corrections noted).

June 6. Notice of settlement filed by General Counsel.

DOCKET ENTRIES—Continued

1934.

June 9. Notice of settlement filed by taxpayer.
June 14. Notice of hearing July 11, 1934 on settlement.
June 19. Consent to settlement filed by taxpayer.
June 26. Decision entered—Division 2, Mr. Trammell.
Sept. 13. Petition for review by U. S. Circuit Court of Appeals, 2nd Circuit, with assignments of error filed by General Counsel.
Sept. 26. Proof of service filed by General Counsel (2).

[fol. 3]

Sept. 14. Petition for review by U. S. Circuit Court of Appeals, 9th Circuit, with assignments of error filed by General Counsel.
Sept. 26. Proof of service filed by General Counsel (2).
Oct. 15. Order from 9th Circuit correcting petition for review filed.
Nov. 9. Motion for extension to Jan. 11, 1934 to complete and transmit record filed by General Counsel (2nd Circuit).
Nov. 9. Order enlarging time to Jan. 11, 1934 to complete and transmit record entered (2nd Circuit).
Nov. 9. Motion for extension to Jan. 12, 1934 to complete and transmit record filed by General Counsel (9th Circuit).
Nov. 9. Order enlarging time to Jan. 12, 1934 to complete and transmit record, 9th Circuit, entered.
Dec. 15. Statement of evidence lodged (2nd Circuit).
Dec. 20. Copy of order from 2nd Circuit correcting petition for review filed.
Dec. 24. Motion for extension of 10 days from Dec. 29, 1934 to file objections and proposed amendments to statement of evidence filed by taxpayer.
Dec. 27. Præcipe with proof of service thereon filed (2nd Circuit).

[fol. 4]

Dec. 27. Notice of lodgment of statement and of hearing Jan. 2, 1935 to approve statement filed.
Dec. 27. Motion of Dec. 24, 1934 granted.
Dec. 28. Notice changing hearing date to Jan. 9, 1935.

DOCKET ENTRIES—Continued

1935.

Jan. 9. Motion for extension to March 13, 1935 to complete and transmit record filed by General Counsel (9th Circuit).

Jan. 9. Order enlarging time to 3/13/35 to complete and transmit record, 9th Circuit, entered.

Jan. 9. Motion for extension to March 12, 1935 to complete and transmit record filed by General Counsel (2nd Circuit).

Jan. 9. Order enlarging time to 3/12/35 to complete and transmit record, 2nd Circuit, entered.

Jan. 9. Hearing had before Mr. Van Fossan on approval statement of evidence—statement approved.

Jan. 10. Agreement to statement lodged 12/15/34 filed by taxpayer.

Jan. 10. Statement of evidence approved and ordered filed (2nd Circuit).

Jan. 11. Statement of evidence lodged (9th Circuit).

[fol. 5] BEFORE UNITED STATES BOARD OF TAX APPEALS

[Title omitted]

PETITION

The above named Petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Rev-nue in his notice of deficiency, IT:-AR:D:CAM-60D, dated March 4, 1930, and as a basis of this proceeding alleges as follows:

I

The Petitioner is a corporation duly organized and existing under and by virtue of the laws of the State of California with its principal place of business in San Francisco, California.

II

The notice of deficiency, a copy of which is attached hereto, marked "Exhibit A" was mailed to Petitioner on or about March 4, 1930.

III

The taxes in controversy are income taxes for the calendar years 1924 to 1926, inclusive, as follows:

[fol. 6]

1924	$26,293.40
1925	187,883.90
1926	133,333.99
Total	$347,511.29

IV

The determination of tax set forth in said notice of deficiency is based upon the following errors:

1. The Respondent in determining the Petitioner's net taxable income failed and neglected to allow as a deduction a reasonable sum for exhaustion, wear and tear and obsolescence on Petitioner's depreciable assets used in its trade or business.

2. The Respondent in determining Petitioner's net taxable income for the year 1924 failed and neglected to allow as a deduction the sum of $2,200.00, which was expended by Petitioner during the year in the conduct of its business.

3. The Respondent erred in failing to allow Petitioner to deduct from its gross income the following sums representing discount and premiums on bonds issued by the Petitioner which were retired during the years 1924 to 1926, inclusive, as follows:

1924	$137,272.57
1925	892,829.19
1926	10,101.19

[fol. 7] 4. The Respondent erred in neglecting and refusing to consolidate the income and/or accounts of the Petitioner with those of other corporations before computing its tax liability in accordance with the provisions of Section 240 of the Revenue Acts of 1924 and 1926.

V

The facts upon which the Petitioner relies as a basis for this proceeding are as follows:

(a) The Petitioner, the Great Western Power Company of California is now and for a number of years past has been a corporation duly organized and existing under and by virtue of the laws of the State of California; Petitioner since its organization has been and now is a public utility engaged in the business of generating and distributing light, heat and power, having its principal place of business in San Francisco, California, and as a public utility has been and now is subject to the regulatory powers conferred by statute of the State of California upon the State Railroad Commission.

(b) The Petitioner, the Western Power Corporation, a New York corporation, and the California Electric Generating Company, a California Corporation, were affiliated during the year 1924. The Western Power Corporation above referred to duly filed a consolidated income tax return for the calendar year 1924, under the provisions of the Revenue Act of 1924, for itself and the Petitioner and the California Electric Generating Company; the Petitioner for said year 1924 filed Form 1122.

[fol. 8] For the year 1925, the Petitioner and the California Electric Generating Company were affiliated; the Petitioner duly filed a consolidated income tax return under the provisions of the Revenue Act of 1924 for itself and the said California Electric Generating Company.

For the year 1926 the Petitioner, the California Electric Generating Company and the Napa Valley Electric Company were affiliated; and the Petitioner filed a consolidated return for itself and these two companies in accordance with the provisions of the Revenue Act of 1926.

(c) During the years 1924, 1925 and 1926 and for many years prior thereto the Great Western Power Company of California or its predecessor, the Great Western Power Co. owned all of the common stock of the California Electric Generating Company amounting to $5,000,000.00 par value; at the same time the preferred stock in the amount of $2,500,000.00 par value was outstanding in the hands of the public. During all of said years there was in effect a guarantee by the Great Western Power Company of California or its predecessor, the Great Western Power Co. for the payment of dividends on the preferred stock and interest and principal on the bonds of the California Electric Gen-

erating Company. During all of said time the only property owned by the California Electric Generating Company was the Oakland Steam plant which was and is possessed and operated by the Great Western Power Company of California under a lease which provides that the Great Western Power Company of California pay as rental an [fol. 9] amount equivalent to the dividends on the preferred stock, interest and sinking fund requirements on the bonds, taxes and assessments against the Generating Company or its properties, including income taxes and an amount sufficient to maintain the corporate existence of the California Electric Generating Company. The officers and directors of the California Electric Generating Company have always been substantially the same as those of the Great Western Power Company of California or the Great Western Power Co. California Electric Generating Company has never had separate offices or employees of its own. All its records are kept in the offices of the Great Western Power Company of California by employees of the latter company and the plant is operated and managed by the employees of the said Great Western Power Company of California. The entire output of the plant is taken by the Great Western Power Company of California on the premises. The California Electric Generating Company owns no transmission or distributing lines and has no franchise or permit from the City of Oakland or any other city or county to use the public streets and highways for the purpose of transmitting and distributing electric energy. The plant is operated and has always been an integral part of the Great Western Power Company's system, having been constructed originally for the sole purpose of making steam standby service available to the Great Western Power Co. consumers. In case of cancellation of the lease the California Electric Generating Company would own a steam plant without an organization to operate same and without consumers and a means of disposing of the output of the [fol. 10] plant. The California Electric Generating Company is controlled directly or indirectly by the same interests within the purview of Section 240 of the Revenue Acts of 1924 and 1926.

(d) The Petitioner during the years 1924, 1925 and 1926 was the owner and possessor of depreciable assets used in its trade or business, including among others, dams, power

and transmission lines, generating plants, etc. of a total cost as follows:

1923	$41,930,042.12
1924	45,373,613.84
1925	48,037,468.86
1926	53,044,701.49

During these years the Petitioner sustained a loss on said assets due to exhaustion, wear and tear and obsolescence in the total sum of:

1924	$1,158,940.29
1925	1,259,066.43
1926	1,385,184.57

which are reasonable sums to be allowed as deductions in determining Petitioner's net taxable income. In lieu of the amounts indicated as a reasonable allowance for exhaustion, wear and tear for the various years the Respondent allowed but $528,017.63 for the year 1924, $547,742.06 for the year 1925 and $583,069.01 for the year 1926.

(e) During the year 1924 the Petitioner paid to the Industrial Association the sum of $720.00, to the United [fol. 11] States Chamber of Commerce $1,000.00 and to Californians, Inc., $500.00, all of which are ordinary and necessary expenses of operation of the Petitioner's trade or business.

(f) During the year 1924 the Petitioner redeemed an issue of General Lien 8% bonds. The unamortized discount on these bonds at time of redemption amounted to $137,272.57 which the Respondent erroneously and illegally refused to allow as a deduction in computing the Petitioner's net taxable income.

During the year 1925 the Petitioner redeemed an issue of First and refunding series "B" 7% bonds. The unamortized discount and premium paid on redemption on these bonds amounted to $892,829.14 which the Respondent erroneously and illegally refused to allow as a deduction in computing Petitioner's net taxable income for said year.

During the year 1926 the Petitioner retired through sinking funds a certain number of its outstanding bonds. The unamortized discount and premium paid on the retirement of said bonds amounted to $10,101.19, which the Respondent

erroneously and illegally failed and refused to allow as a deduction from its net taxable income.

Wherefore, the Petitioner prays that the Board hear and determine this appeal and render judgment in accordance with the foregoing.

Thomas R. Dempsey, A. Calder Mackay, Attorneys for Petitioner, 508 Security Building, Los Angeles, California.

[fol. 12] *Duly sworn to by L. A. Reynolds. Jurat omitted in printing.*

[fol. 13] EXHIBIT A, ANNEXED TO FOREGOING PETITION

[Copy]

Treasury Department, Washington

Office of Commissioner of Internal Revenue

March 4, 1930.

Great Western Power Company of California, 530 Bush Street, San Francisco, California

SIRS:

In accordance with Section 274 of the Revenue Act of 1926, you are advised that the determination of your tax liability for the years 1924, 1925 and 1926 discloses a deficiency of $347,511.29, as shown in the statement attached.

The section of the law above mentioned allows you to petition the United States Board of Tax Appeals within sixty days (not counting Sunday as the sixtieth day) from the date of the mailing of this letter for a redetermination of your tax liability.

However, if you do not desire to petition, you are requested to execute the inclosed Form 866 and forward both original and duplicate to the Commissioner of Internal Revenue, Washington, D. C. for the attention of IT:C:P-7. The signing of this agreement form will expedite the closing of your return by permitting an early assessment of [fol. 14] any deficiencies and preventing the accumulation

of interest charges, since the interest period terminates thirty days after filing the agreement form, or on the date assessment is made, whichever is earlier; whereas if no agreement is filed, interest will accumulate to the date of assessment of the deficiencies.

Respectfully, Robt. H. Lucas, Commissioner, by (Signed) David Burnet, Deputy Commissioner.

Enclosures: Statement. Form 866. Form 882. Schedules 1 to 15, inclusive.

[fol. 15]

IT:AR:D.
CAM-60D.

Statement of Returns Examined and Resulting Tax Liability

Returns Examined

Parent Company	Years	Forms
Great Western Power Company of California, San Francisco, California	1924	1122
	1925	1120 Consolidated
	1926	1120 Consolidated
Subsidiaries:		
Napa Valley Electric Company, San Francisco, California	1926	None
Great Western Power Company		
City Electric Company		
Consolidated Electric Company		
United Light and Power Company, (New Jersey)	1924)	
United Light and Power Company (California)	1925)	Inactive
Consumers Light and Power Company	1926)	
Equitable Light and Power Company		
Southside Light and Power Company		
Central Oakland Light and Power Company		

[fol. 16]

Tax Liability

Great Western Power Company of California

Years	Corrected Tax Liability	Tax Previously Assessed	Deficiency
1924	$138,104.49	$111,811.09	$26,293.40
1925	187,883.90	None	
1926	245,940.16	112,606.17	133,333.99
Total	$571,928.55	$224,417.26	$347,511.29

Napa Valley Electric Company

1926	850.06	None	850.06
Grand Total	$572,778.61	$224,417.26	$348,361.35

The adjustments producing the above-stated results are shown in the attached Schedules 1 to 15 inclusive.

Consents, which will expire December 31, 1930, except as extended by the provisions of Section 277(b) of the

Revenue Act of 1926 are on file for the years 1924 and 1925.

During the taxable year 1924, your company was not affiliated with the Western Power Corporation within the purview of Section 240 of the Revenue Act of 1924 for the reason that at least 95 per cent of your capital stock was not owned by that company, and during the taxable years 1924, 1925 and 1926, your company and the California Electric Generating Company were not affiliated [fol. 17] within the purview of Section 240 of the Revenue Acts of 1924 and 1926 for the reason that your company did not own at least 95 per cent of the capital stock of that company.

The consolidated tax assessed and corrected tax liability has been allocated to the various companies on the basis of the net income properly assignable to each as provided in Section 240 of the Revenue Acts of 1924 and 1926.

Schedule 1

Year ended December 31, 1924

Net Income

Net income as disclosed by return (Western Power Corporation)		$923,203.47
As corrected		1,104,835.88
Net adjustment		181,632.41
Unallowable deductions and additional income:		
(a) Donations	$2,595.00	
(b) Depreciation	139,547.05	
(c) Franchise Taxes	9,075.93	
(d) Premium on bonds retired	137,272.57	
Total		288,490.55
[fol. 18]		
Nontaxable income and additional deductions:		
(e) Repairs, etc., allowed as deductions	$91,494.29	
(f) Valuation expense	15,363.85	
		106,858.14
Net adjustment as above		$181,632.41

Schedule 2

Explanation of Items Changed

(a) The following donations are disallowed as deductions:	
Industrial Association	$720.00
United State Chamber of Commerce—Contribution	1,000.00
Californians, Inc.	500.00
Prohibition Fund	375.00
Total	$2,595.00

(b) Depreciation not on books, claimed on return is disallowed. The Bureau holds that the depreciation taken on books and allowed by the California Railroad Commission is a reasonable depreciation.

(c) Adjustment for accrual of franchise tax as shown in your brief is allowed.

[fol. 19]

(d) The Bureau holds that premiums paid on bonds retired are not allowable deductions from income.
(e) Repairs, etc., claimed in your brief allowed in the amount of $91,494.29.
(f) Valuation expense allowable as a deduction as claimed in your brief.

Schedule 3

Computation of Tax

Income Tax

Net income for taxable year (Schedule 1)		$1,104,835.88
Income tax 12½ per cent		138,104.49
Total previously assessed:		
Consolidated Return Western Power Company, Account #405,628, April, 1925	$136,611.47	
Less: Allocated to other companies on basis of income reported	24,800.38	
Balance		111,811.09
Additional tax to be assessed		$26,293.40

[fol. 20]

Schedule 4

Year ended December 31, 1925

Net Income

Net loss as disclosed by return		$165,199.74
As corrected—net income		1,445,260.75
Net adjustment		$1,610,460.49
Unallowable deductions and additional income:		
(a) Depreciation	$789,405.44	
(b) Premiums on bonds retired	892,829.14	
Total		1,682,234.58
Nontaxable income and additional deductions:		
(c) Valuation expense	$71,530.11	
(d) Depreciation on items expensed	243.98	
Total		71,774.09
Net adjustment as above		$1,610,460.49

[fol. 21]

Schedule 5

Year ended December 31, 1925

Explanation of Items Changed

(a) See explanation, Schedule 2 (b).
(b) See explanation, Schedule 2 (d).
(c) See explanation, Schedule 2 (f).
(d) Depreciation on items expensed disallowed.

Buildings, alterations $2,078.21 at 10 per cent	$207.82
Furniture $361.57 at 10 per cent	36.16
Total	243.98

Schedule 6

Computation of Tax

Income Tax

Net income for taxable year (Schedule 4)		$1,445,260.75
Income tax 13 per cent		187,883.90
Account # 400,600, September, 1926	$5,088.10	
Less: Allocated to other companies on basis of income reported	5,088.10	
Balance		None
Additional tax to be assessed		$187,883.90

[fol. 22]

Schedule 7

Year ended December 31, 1926

Net Income

Net income as disclosed by return		$835,930.78
As corrected		1,821,778.94
Net adjustment		985,848.16
Unallowable deductions and additional income:		
(a) Depreciation	$883,899.83	
(b) Valuation expense	86,893.96	
(c) Alterations building Spring Valley	361.57	
(d) Furniture and Fixtures	3,335.91	
(e) Miscellaneous prior year items	1,562.56	
(f) Premium on bonds retired	10,101.19	
Total		$986,155.02
Nontaxable income and additional deductions:		
(g) Depreciation		306.86
Net adjustment as above		$985,848.16

[fol. 23]

Schedule 8

Explanation of Items Changed

(a) Depreciation claimed in excess of that shown on your books, not being deemed reasonable, is disallowed pending final determination of this question for the prior years.

(b) Valuation expense of prior years claimed as a deduction during this year is disallowed.

1924	$15,363.85	
1925	71,530.11	
Total		86,893.96

(c) and (d) Capital items expended.

(e) Prior year items claimed in 1926.

(f) See explanation, Schedule 2 (d).

(g) Depreciation on items (c) and (d).

(c) Building alterations	
(1925 cost) $361.57 at 10 per cent	36.16
(d) Furniture and Fixtures	
(1925 cost) 2,078.21 at 10 per cent	207.82
(1926 cost) 1,257.70 at 5 per cent	62.88
Total	306.86

[fol. 24]

Schedule 9

Napa Valley Electric Company

Net Income

Net loss as disclosed by return	$2,253.80
As corrected—net income	6,296.78
Net adjustment	$8,550.58
Unallowable deductions and additional income:	
(a) Depreciation (see Schedule 8 [a])	$8,550.58

Schedule 10

Great Western Power Company of California

Consolidated Net Income—1926

Net income as corrected:		
Great Western Power Company of California (Schedule 7)	1,821,778.94	
Napa Valley Electric Company (Schedule 9)	6,296.78	
Consolidated Net Income Corrected		$1,828,075.72

[fol. 25]

Schedule 11

Computation of Tax—1926

Income Tax

Net income for taxable year (Schedule 10)	$1,828,075.72
Income tax 13½ per cent	246,790.22

Schedule 12

Allocation of Original Tax

Account # 402,966, May, 1927

Name of Company	Income	Amount
Great Western Power Company of California	$835,930.78	$112,606.1
Napa Valley Electric Company	Loss	None
Total Group I	$835,930.78	$112,606.17
Non-affiliated:		
California Electric Generating Company	204,388.65	27,532.69
Grand Total	$1,040,319.43	140,138.86

[fol. 26]

Schedule 13

Allocation of Corrected Tax

Name of Company	Income	Amount
Great Western Power Company of California	$1,821,778.94	$245,940.16
Napa Valley Electric Company	6,296.78	850.06
Totals	$1,828,075.72	$246,790.22

Schedule 14

Computation of Tax

Income Tax

Total Tax Assessable—allocated, Schedule 13	$850.06
Total previously assessed—allocated, Schedule 12	None
Additional tax to be assessed	$850.06

[fol. 27]

Schedule 15

Great Western Power Company of California

Computation of Tax

Income Tax

Total tax assessable—allocated, Schedule 13	$245,940.16
Total previously assessed—allocated, Schedule 12	112,606.17
Additional tax to be assessed	$133,333.99

Treasury Department, Washington

March 4, 1930.

Office of Commissioner of Internal Revenue

Refer to IT:AR:D
CAM-60D

Great Western Power Company of California, 530 Bush Street, San Francisco, California.

SIRS:

Your claim for the refund of $5,088.10, corporation income tax for the year 1925, has been examined and will [fol. 28] be rejected for the reason that an audit of your return discloses a tax liability equal to the amount assessed.

In arriving at your tax liability, due consideration was given to the statement in your claim. The basis of the adjustments in the audit has been made the subject of a separate communication from the Bureau.

The rejection of your claim will officially appear on the next schedule for your district to be approved by the Commissioner.

Respectfully, David Burnet, Deputy Commissioner, by (Signed) H. B. Robinson, Head of Division.

Treasury Department, Washington

March 4, 1930.

Office of Commissioner of Internal Revenue

Great Western Power Company of California, 530 Bush Street, San Francisco, California.

SIRS:

Your claim for the refund of $21,467.50, corporation income tax for the year 1926, has been examined and will be rejected for the reason that an audit of your return discloses a tax liability equal to the amount assessed.

[fol. 29] In arriving at your tax liability, due consideration was given to the statement in your claim. The basis of the adjustments to the audit has been made the subject of a separate communication from the Bureau.

The rejection of your claim will officially appear on the next schedule for your district to be approved by the Commissioner.

Respectfully, David Burnet, Deputy Commissioner, by (Signed) H. B. Robinson, Head of Division.

BEFORE UNITED STATES BOARD OF TAX APPEALS

[Title omitted]

ANSWER

The Commissioner of Internal Revenue by his attorney, C. M. Charest, General Counsel, Bureau of Internal Revenue, for answer to the petition filed in the above entitled appeal, admits and denies as follows:

[fol. 30] I. Admits the allegations contained in paragraph I of the petition.

II. Admits the allegations contained in paragraph II of the petition, except that it is averred that on page 1 of the statement attached to the deficiency letter petitioner's copy has omitted to insert the amount of $187,883.90 as the deficiency determined against the petitioner for the year 1925.

III. Admits the allegations contained in paragraph III of the petition.

IV. Denies the allegations contained in paragraph IV of the petition, subparagraphs 1 to 4, inclusive.

V. Admits the allegations contained in subparagraph (a) of paragraph V of the petition. Denies all the allegations of fact contained in subparagraphs (b), (c), (d), (e) and (f) of paragraph V of the petition, which are inconsistent with the deficiency notice referred to in paragraph II of this petition.

Denies generally and specifically each and every allegation contained in the taxpayer's petition not hereinbefore admitted, qualified or denied.

Wherefore, it is prayed that the taxpayer's appeal be denied.

C. M. Charest, General Counsel, Bureau of Internal Revenue.

Of Counsel: F. R. Shearer, Special Attorney, Bureau of Internal Revenue.

[fol. 31] BEFORE UNITED STATES BOARD OF TAX APPEALS

[Title omitted]

FIRST AMENDED PETITION

By leave of the Board first had and obtained, petitioner files this as its first amended petition appealing from the respondent's determination as set forth in his deficiency letter dated March 4, 1930, symbols IT:AR:D:CAM-60D, and as a basis for this proceeding alleges as follows:

I

Petitioner is a corporation duly organized and existing under and by virtue of the laws of the State of California with its principal place of business in San Francisco, California.

II

The notice of deficiency, copy of which is attached to the original petition, was mailed to petitioner on or about March 4, 1930.

III

The taxes in controversy are income taxes for the calendar years 1924 to 1926, inclusive, as follows:

[fol. 32]	1924	$26,293.40
	1925	187,883.90
	1926	133,333.99
	Total	$347,511.29

IV

The determination of the tax set forth in the notice of deficiency is based upon the following errors:

(1) In determining petitioner's net taxable income for each of the years 1924, 1925 and 1926, the respondent erred in failing to allow as a deduction a reasonable sum for the exhaustion, wear, tear and obsolescence of petitioner's assets used in its trade or business.

(2) In determining petitioner's net taxable income for the year 1924, the respondent erred in failing to allow as a deduction the sum of $1,220.00 expended by petitioner during said year in the conduct of its business.

(3) In determining petitioner's net taxable income for the year 1925, the respondent erred in failing to allow as a deduction the sum of $26,558.76 interest paid during the year.

(4) In determining petitioner's net taxable income for the year 1926, the respondent erred in failing to allow as a deduction:

[fol. 33] (a) The sum of $11,989.68 representing the loss sustained by reason of the purchase and retirement of certain of petitioner's outstanding bonds.

(b) The sum of $202.50 representing the loss sustained by reason of the purchase of certain bonds of the California Electric Generating Company.

(5) In determining petitioner's net taxable income for the year 1924, the respondent erred in failing to allow as deductions:

(a) The sum of $243,335.06 being the loss sustained on the conversion of $2,354,500.00 face value of petitioner's General Lien 8% bonds into a like amount of petitioner's Series B 7% bonds.

(b) The sum of $8,552.20, being the loss sustained on the cash redemption of $134,500.00 face value of General Lien 8% bonds.

(6) In determining petitioner's net taxable income for the year 1925, the respondent erred in failing to allow as a deduction the sum of $868,189.12, being the loss sustained on the cash redemption of $7,422,600.00 face value of petitioner's Series B 7% bonds.

(7) The respondent erred in determining that only $111,811.09 of the total tax paid for the year 1924 on the consolidated return filed by the Western Power Corporation and affiliated companies is allocable to petitioner.

(8) The respondent erred in failing to allow an operating loss in the sum of $134,135.88 or a greater amount suffered [fol. 34] by petitioner in its trade or business for the year 1925 to be carried forward as a deduction in determining petitioner's net taxable income for the year 1926.

V

The facts upon which petitioner relies as the basis for this proceeding are as follows:

(a) At all times herein material petitioner was a public utility corporation engaged in the generation, sale, and distribution of electricity. As a public utility corporation petitioner was at all times herein material subject to the jurisdiction and control of the California State Railroad Commission and kept its books on the accrual basis in accordance with the classification of accounts prescribed by said Commission. Petitioner's income tax returns for the years herein involved were made on the accrual basis.

(b) During the years indicated below petitioner was the owner and possessor of certain depreciable assets upon

which it sustained depreciation due to exhaustion, wear, tear and obsolescence in the amounts shown below:

1924	$1,152,571.00
1925	1,234,772.00
1926	1,378,690.00

(c) During the year 1924 petitioner paid to the Industrial Association of San Francisco the sum of $720.00 and [fol. 35] to Californians, Inc. the sum of $500.00. Both of these amounts were ordinary and necessary expenses of operation of petitioner's trade or business.

(d) During the year 1925 petitioner issued and sold $6,300,000.00 face value of its Series D 5½% bonds. The effective date of the sale of these bonds was June 10, 1925, but the funds derived from such sale were held by the Bank of America in escrow from June 10, 1925, until August 1, 1925. The difference between the amount of interest which was allowed by the bank on the funds so held and the amount of interest which accrued on the bonds from whose sale such funds were derived was $26,558.76. This sum constitutes interest actually paid by petitioner and as such is allowable as a deduction from gross income.

(e) During the year 1926 petitioner purchased for cash and retired certain of its outstanding Series A 6%, Series C 6%, and Series D 5½% bonds. The premiums paid on these bonds amounted to $3,445.15 and the unamortized discount and expense applicable thereto at the date of retirement was $8,544.53. Also during the year 1926 petitioner purchased $28,000.00 face value of the California Electric Generating Company's bonds from the public for $28,202.50 and, pursuant to a rental agreement with the said Generating Company, turned such bonds over to that company at their face value. By reason of this transaction petitioner sustained an actual loss of $202.50.

(f) During the year 1921 petitioner issued and sold $2,500,000.00 face value of its General Lien 8% Gold Bonds [fol. 36] dated February 1, 1921, and due February 1, 1936. The discount on the sale of these bonds was $150,000.00 and the expense of issuance was $22,283.54. It was provided in these General Lien bonds that they were to be secured by the deposit with the General Lien trustees of an equal face amount of petitioner's Series B 7% bonds. The deposit

of the Series B 7's as collateral was actually made during the year 1921. It was also provided in the General Lien bonds that the holders thereof had the option of exchanging such bonds, when and if called, for a like amount of the Series B 7% bonds plus a cash premium of 5%.

On May 8, 1924, petitioner's Board of Directors adopted a resolution calling for redemption on August 1, 1924, all of the General Lien 8% bonds outstanding on the date of the resolution. On August 1, 1924, the holders of $2,354,500.00 face value of the General Lien bonds exchanged them for a like amount of Series B bonds and received in addition to said Series B bonds, a cash premium of $117,725.00. The unamortized discount and expense of issuance applicable to the General Lien bonds so converted amounted to $126,176.97 and the expense of conversion was $1,461.05.

(g) All of the General Lien 8% bonds outstanding on August 1, 1924, which were not converted into Series B 7% bonds were redeemed as of August 1, 1924, for cash, and the holders thereof received, in addition to the face value of their bonds, a cash premium of 5%. The total face value of all General Lien 8% bonds redeemed for cash as of August 1, 1924, was $134,500.00 and the total premium [fol. 37] paid was $6,725.00. The unamortized discount and expense of issuance as of August 1, 1924, applicable to the bonds redeemed for cash was $7,207.82. The expense of redemption applicable to such bonds was $83.46.

(h) During the year 1921 petitioner issued $8,500,000.00 face value of its Series B 7% bonds which were disposed of in the following manner:

$5,000,000.00 face value were deposited with the trustees, under petitioner's General Mortgage Indenture as collateral security for the outstanding General Mortgage 8% bonds;

$2,500,000.00 face value were deposited with petitioner's General Lien trustees as collateral security for the General Lien 8% bonds; and

$1,000,000.00 face value were sold to the public in 1921 at a discount of $100,000.00. The expense of issuing the entire Series B was $49,548.14.

(i) On May 31, 1925, Series B 7% bonds of a total face value of $7,422,600.00 were outstanding in the hands of the public. During the month of June, 1925, Series B 7%

bonds of a total face value of $419,700.00 were purchased for cash at a premium of $43,415.22 and retired; during the month of July, 1925, Series B bonds of a total face value of $257,400.00 were purchased for cash at a premium of $10,863.50 and retired; and on August 1, 1925, all of the remaining Series B bonds then outstanding, to wit, $6,745,500.00 face value, were redeemed by the cash payment to the holders thereof of the face value of their bonds plus a premium of 10%. The total premium paid on the August 1, 1925 redemtion amounted to $674,550. The amounts of [fol. 38] unamortized discount and expense of issuance applicable to the bonds purchased and retired in June and July and to the bonds redeemed on August 1, 1925, were respectively: $7,399.61, $4,523.15 and $117,989.72. The total expense incurred in connection with these three transactions was $9,447.92.

(j) The amounts of cash necessary for the June and July purchases were taken from the general funds in petitioner's treasury; so also was the amount required for the payment of the expense.

The amount of cash necessary for the August 1, 1925 redemption was $7,420,050.00. Of this amount, the sum of $6,650,000.00 was derived from the issuance and sale in June and July of petitioner's Series D 5½% bonds of a face value of $7,000,000.00; the remainder, $770,050.00, was taken from the general funds in petitioner's treasury.

(k) The Series D 5½% bonds were sold as follows:

Date	Purchaser	Par value	Discount
March, 1925	Public	$1,500,000.00	$112,500.00
June 10, 1925	Public	6,300,000.00	315,000.00
July 15, 1925	Western Power Corp.	700,000.00	35,000.00
Subsequent to August 1, 1925	Public	1,000,000.00	50,000.00

The total expense of issuing the Series D 5½% bonds, to wit, $47,094.15, was paid out of the general funds in petitioner's treasury.

(l) Petitioner's net income for the year 1924 was included in a consolidated return filed by the Western Power [fol. 39] Corporation and affiliated companies. The respondent, after determining that petitioner was not affiliated with any other corporation during the year 1924, incorrectly allocated to petitioner only $111,811.09 of the total

tax paid on the consolidated return, whereas the sum of $114,486.47 is the true amount of the tax paid which is properly allocable to petitioner.

(m) During the year 1925 petitioner sustained a net loss in the operation of its trade or business which net loss is computed as follows:

Net Income per deficiency letter		$1,445,260.75
Add:		
Dividends Received	$50.00	
Exempt Interest	2,087.21	2,137.21
Total		$1,447,397.96
Deduct:		
Additional Depreciation	$686,785.96	
Interest Paid	26,558.76	
Loss on bonds redeemed	868,189.12	1,581,533.84
Net Loss		$134,135.88

Petitioner alleges that it has overpaid its income taxes for the years here under appeal and prays that the amounts of such overpayments be refunded to it.

Wherefore, petitioner prays that the Board hear and determine this appeal as herein amended and render judgment accordingly.

Thomas R. Dempsey, A. Calder Mackay, Attorneys for Petitioner, 1104 Pacific Mutual Building, Los Angeles, California.

[fol. 40] *Duly sworn to by L. A. Reynolds. Jurat omitted in printing.*

BEFORE UNITED STATES BOARD OF TAX APPEALS

[Title omitted.]

ANSWER TO FIRST AMENDED PETITION

The Commissioner of Internal Revenue by his attorney, E. Barrett Prettyman, General Counsel, Bureau of Internal [fol. 41] Revenue, for answer to the first amended petition

filed September 19, 1933, admits, denies, avers and alleges as follows:

I. Admits the allegations contained in paragraph I of the first amended petition.

II. Admits the allegations contained in paragraph II of the first amended petition, except that it is averred that on page 1 of the statement attached to the deficiency letter petitioner's copy has omitted to insert the amount of $187,883.90 as the deficiency determined against the petitioner for the year 1925.

III. Admits that the taxes in controversy are income taxes for the calendar years 1924, 1925 and 1926 and that the Commissioner determined deficiencies for said years in the amounts set forth in paragraph III of the first amended petition.

IV. (1) Admits that petitioner is entitled to additional deductions for exhaustion, wear, tear and obsolescence of assets used in its trade or business, and avers that the correct amounts thereof are set forth in the stipulation of facts filed with the Board June 5, 1933.

(2) Admits the allegation of error set forth in subparagraph (2) of paragraph IV of the first amended petition.

(3) Admits the allegation of error set forth in subparagraph (3) of paragraph IV of the first amended petition.

[fol. 42] (4) (a) and (b) Denies that the Commissioner erred as alleged in sections (a) and (b) of subparagraph (4) of paragraph IV of the first amended petition.

(5) (a) Denies that the Commissioner erred as alleged in section (a) of subparagraph (5) of paragraph IV of the first amended petition.

(b) Admits the allegation of error set forth in section (b) of subparagraph (5) of paragraph IV of the first amended petition.

(6) Denies the allegations of error set forth in subparagraph (6) of paragraph IV of the first amended petition.

(7) Avers that the correct allocation of tax previously assessed and paid on the consolidated return filed by Western Power Corporation for the year 1924 is set forth in the stipulation of facts filed with the Board June 5, 1933.

(8) Denies the allegation of error set forth in subparagraph (8) of paragraph IV of the first amended petition.

V. (a), (b) and (c) Admits all the allegations of fact contained in subparagraphs (a), (b) and (c) of paragraph V of the first amended petition.

(d) Admits that during the year 1925 petitioner issued and sold certain of its Series D 5½% bonds; that certain funds derived therefrom remained on deposit with a bank from the effective date of the bonds until August 1, 1925; [fol. 43] that the amount of interest which accrued on such bonds from the effective date thereof until August 1, 1925, exceeded by the amount of $26,558.76 the interest which was allowed by the bank on the funds so held; and that this sum constitutes an allowable deduction from gross income for the year 1925.

(e), (f) and (g) Admits all the allegations of fact contained in subparagraphs (e), (f) and (g) of paragraph V of the first amended petition. Respondent further avers and alleges that the unamortized discount and expense, premiums paid, and expense of conversion applicable to the $2,354,500 General Lien bonds converted into and exchanged for Series B 7% bonds were not charged to profit and loss on petitioner's books of account, but were transferred to "Discount and Expense Series B account General Lien" to be amortized over the remaining life of the Series B 7% bonds.

(h) Admits that during the year 1921 petitioner made provision for the issuance of a total of $8,500,000 face value of its Series B 7% bonds of which $5,000,000 face value were deposited with the trustees under petitioner's General Mortgage Indenture as collateral security for its outstanding General Mortgage 8% bonds; $2,500,000 face value were deposited with the trustees under petitioner's General Lien Indenture as collateral security for its General Lien 8% bonds; and $1,000,000 face value were issued to the public in 1921 at a discount of $100,000. Admits that the expense of issuing the entire $8,500,000 face value of Series B bonds was $49,548.14.

[fol. 44] (i), (j) and (k) Admits that early in 1925 petitioner's Series B 7% bonds of a total face value of $7,422,600 were outstanding in the hands of the public; and that

during the year 1925 all of said Series B 7% bonds were retired. Admits that during the year 1925 the petitioner issued and disposed of its Series D 5½% bonds dated February 1, 1925, maturing February 1, 1955, bearing interest at 5½% per annum and secured under the same mortgage indenture as petitioner's Series B 7% bonds above referred to, as follows:

Date	Par value	Discount
March, 1925	$1,500,000	$112,500
June 10, 1925	6,300,000	315,000
July 15, 1925	700,000	35,000
Subsequent to August 1, 1925	1,000,000	50,000

Admits that incident to the issuance of said Series D 5½% bonds petitioner expended the additional amount of $47,094.15. Avers and alleges that the retirement of said Series B 7% bonds and the issuance of said Series D 5½% bonds were dependent one upon the other and constituted part of a refunding or refinancing program whereby petitioner refunded a portion of its bonded indebtedness by reducing the interest rate thereof and extending the maturity date. Admits that at least $6,500,000 used for the retirement of said Series B bonds was derived from the issuance of petitioner's Series D 5½% bonds, and avers that whatever funds may have been taken from petitioner's [fol. 45] treasury for the purpose of retiring said Series B bonds were reimbursed within the year 1925 from funds derived from the aforesaid issuance of Series D 5½% bonds. Admits that the amounts of premiums paid and expense incurred in connection with the retirement of said Series B bonds were $728,828.72 and $9,447.92, respectively; and that the unamortized discount and expense of issuance applicable to such Series B bonds, to their respective dates of retirement, aggregated $129,912.48. Denies all other allegations of fact contained in subparagraphs (i), (j) and (k) of paragraph V of the first amended petition. Respondent further avers and alleges that the unamortized discount and expense, premiums paid, and expense of retirement applicable to the Series B 7% bonds retired in June, July and August, 1925 (including the unamortized portion of similar amounts applicable to General Lien 8% bonds converted into Series B 7% bonds in 1924) were not charged to profit and loss on petitioner's books of account,

but were transferred to "Discount and Expense Series D 5½'s account Series B 7's" to be amortized over the remaining life of the Series D 5½% bonds.

(l) Admits that for the calendar year 1924 petitioner's reported income was included in a consolidated return in the name of Western Power Corporation and affiliated companies, that the Commissioner disallowed affiliation and allocated to petitioner $111,811.09 of the amount shown as the tax assessed and paid on the basis of said consolidated return. Admits that pursuant to an agreement between the interested corporations the correct amount allocable to petitioner is $114,486.47.

[fol. 46] (m) Denies all the allegations of fact contained in subparagraph (m) of paragraph V of the first amended petition.

Denies generally and specifically each and every allegation contained in the taxpayer's first amended petition not hereinbefore admitted, qualified or denied.

Wherefore, it is prayed that petitioner's appeal be denied, and (in the alternative in the event it be found that the Commissioner allowed deductions in any of the years 1924, 1925 and 1926 on account of premiums, discount and expense on petitioner's bonded indebtedness which should have been allowed in some different year) that the Board redetermine the correct amounts of the deficiencies for each of said years. The Commissioner hereby makes claim to any increased deficiency which may result from such redetermination.

(Sgd.) E. Barrett Prettyman, General Counsel, Bureau of Internal Revenue.

Of Counsel: F. R. Shearer, Special Attorney, Bureau of Internal Revenue.

[fol. 47] Before United States Board of Tax Appeals

[Title omitted]

Settlement Under Rule 50

Comes now the Commissioner of Internal Revenue by his attorney, Robert H. Jackson, General Counsel, Bureau

of Internal Revenue, and files herewith, as the basis for the entry of the Board's order of redetermination, a recomputation of the tax liability of the Great Western Power Company of California for the years 1924, 1925 and 1926 which is believed to be in accordance with the report of the Board promulgated April 26, 1934.

This recomputation is submitted without prejudice to the right of the Commissioner to contest the correctness of the Board's decision as provided by statute.

(Signed) Robert H. Jackson, General Counsel, Bureau of Internal Revenue.

Of Counsel: F. R. Shearer, Special Attorney, Bureau of Internal Revenue.

[fol. 48]

Statement

IT:AR:BTA-Recomp.
DGJ.

Returns Examined

Parent Company	Year	Form
Great Western Power Company of California, San Francisco, California	1924	1122
	1925	1120 (Consolidated)
	1926	1120 (Consolidated)
Subsidiaries:		
Napa Valley Electric Company, San Francisco, California	1926	None
Great Western Power Company		Inactive
City Electric Company		
United Light and Power Company (New Jersey)		
United Light and Power Company (California)		
Consumers Light and Power Company		
Equitable Light and Power Company		
Southside Light and Power Company		
Central Oakland Light and Power Company		

Income Tax Liability

Great Western Power Company of California, B. T. A. Docket No. 48617

Year	Income Tax Liability	Income Tax Assessed	Deficiency	Over-assessment
1924	$28,396.91	$114,486.47		$86,089.56
1925	None	None	None	None
1926	119,341.05	112,606.17	$6,734.88	
Totals	$147,737.96	$227,092.64	$6,734.88	$86,089.56

[fol. 49] The adjustments producing the above-stated result are shown in the attached schedules 1 to 14, inclusive, and have been made in accordance with the decision of the United States Board of Tax Appeals, Docket No. 48617.

Year ended December 31, 1924

Great Western Power Company of California

Schedule 1

Adjustments to Net Income

Net income as disclosed by Bureau letter of March 4, 1930		$1,104,835.88
As correct		227,175.25
Net adjustment as computed below		$877,660.63
Nontaxable income and additional deductions:		
(a) Adjustment of depreciation	$624,553.37	
(b) Premiums paid unamortized discount and expense	251,887.26	
(c) Contributions	1,220.00	
Net adjustment as above		$877,660.63

[fol. 50]

Schedule 2

Explanation of Items

(a) $624,553.37 additional depreciation has been allowed as a deduction in accordance with the decision of the United States Board of Tax Appeals, Docket No. 48617. The amount is arrived at as follows:

Depreciation sustained	$1,152,571.00
Previously allowed	528,017.63
Additional amount allowed	$624,553.37

(b) Premiums paid, unamortized discount and expense on retirement of bonds has been allowed as a deduction in accordance with the decision of the United States Board of Tax Appeals, Docket No. 48617. The amount is arrived at as follows:

Bonds retired August 1, 1924, face value		$2,354,500.00
Premiums paid		$117,725.00
Unamortized discount		126,176.97
Expense		1,461.05
Total amount allowable		$245,363.02

[fol. 51]

Less:		
Previously allowed		2,027.93
Additional amount allowed		$243,335.06
Bond retired on August 1, 1924, face value	$134,500.00	
Premiums paid	$6,725.00	
Unamortized discount	7,207.82	
Expense	33.46	
Total amount allowable	$14,016.28	
Previously allowed	5,464.08	
Additional amount allowed		8,552.20
Total additional amount allowed		$251,887.26

(c) $720.00 contributions to the Industrial Association of San Francisco and $500.00 to the Californians, Incorporated, comprising a total of $1,220.00 has been allowed as a deduction in accordance with the decision of the United States Board of Tax Appeals, Docket No. 48617.

Schedule 3

Computation of total tax for the Calendar Year ended December 31, 1924

	Net income	Tax
Net income, schedule (1)	$227,175.25	
Exemption	None	
Taxable at 12½%	$227,175.25	$28,396.91
[fol. 52] Tax previously assessed on consolidated return, Account No. 405628	$136,611.47	
Tax allocated to other companies as stipulated	22,125.00	
Net amount previously assessed		114,486.47
Overassessed		$86,089.56

Year Ended December 31, 1925

Schedule 4

Adjustments to Net Income

Net income as disclosed by Bureau letter of March 4, 1930		$1,445,260.75
As corrected (net loss)		(136,273.09)
Net adjustment as computed below		$1,581,533.84
Nontaxable income and additional deductions:		
(a) Adjustment of depreciation	$686,785.96	
(b) Premiums paid, unamortized discount and expense	868,189.12	
Net adjustment as above		$1,581,533.84
(c) Interest paid	26,558.76	

[fol. 53] Schedule 5

Explanation of Items

(a) 686,785.96 additional depreciation has been allowed as a deduction in accordance with the decision of the United States Board of Tax Appeals, Docket No. 48617. The amount is arrived at as follows:

Depreciation sustained		$1,234,772.00
Previously allowed	($547,742.06	
	(243.98	547,986.04
Additional amount allowed		$686,785.96

(b) Premiums paid, unamortized discount and expense on retirement of bonds has been allowed as a deduction in accordance with the decision of the United States Board of Tax Appeals, Docket No. 48617. The amount is arrived at as follows:

Bonds retired in 1925 series B, 7's at face value of	$7,422,600.00
Premiums paid	$728,828.72
Unamortized discount	129,912.48
Expense	9,447.92
Total amount allowed	$868,189.12

(c) $26,538.76 interest paid has been allowed as a deduction in accordance with the decision of the United States Board of Tax Appeals, Docket No. 48617.

[fol. 54] Schedule 6

Computation of Total Tax for the Calendar Year Ended December 31, 1925

	Net income	Tax
Net loss, schedule (4)	($136,273.09)	
Taxable amount	None	None
Tax previously assessed on consolidated return, account No. 400600	$5,088.10	
Tax allocated to other companies as stipulated	5,088.10	
Net amount assessed		None
Deficiency		None

Year Ended December 31, 1926

Schedule 7

Adjustments to Net Income

Net income as disclosed by Bureau letter of March 4, 1933		$1,821,773.94
As corrected		1,018,143.61
Net adjustment as computed below		$803,635.33
[fol. 55] Unallowable deductions and additional income:		
(a) Adjustment for 1924 amortized discount		$8,735.78
Nontaxable income and additional deductions:		
(b) Adjustment of depreciation	$800,442.93	
(c) Loss on retirement of bonds	11,928.18	
Total		812,371.11
Net adjustment as above		803,635.33

Schedule 8

Explanation of Items

(a) $8,735.78 has been restored to income in 1926, due to having been included in the total amount of $245,363.02 allowed as a deduction in the year 1924.

(b) $800,442.93 additional depreciation has been allowed as a deduction in accordance with the decision of the United States Board of Tax Appeals, Docket No. 48617. The amount is arrived at as follows:

[fol. 56] Depreciation sustained		$1,378,690.00
Previously allowed	($577,940.21	
	(306.86	578,247.07
Additional amount allowed		$800,442.93

Explanation of Items

(c) Loss on purchase and retirement of Company's own bonds and other securities has been allowed in accordance with the decision of the United States Board of Tax Appeals, Docket No. 48617. The amount is arrived at as follows:

Loss on bonds retired:		
Series A 6's		$4,187.31
Series C 6's		4,542.32
Series D 5½'s		3,260.05
Total		$11,989.68
Gain on purchase of Cons. General Mortgage bonds	$234.00	
Central Oakland Light	30.00	
Total	$264.00	
Loss on purchase of California Electric Gen. bonds	202.50	
Net gain		61.50
Loss allowed		$11,528.18

[fol. 57] Napa Valley Electric Company

Year Ended December 31, 1926

Schedule 9

Adjustments to Net Income

Net income as disclosed by Bureau letter of March 4, 1930	$6,296.78
As corrected	5,498.67
Net adjustment as computed below	$ 798.11
Nontaxable income and additional deductions:	
(a) Additional depreciation allowed	$ 798.11

Schedule 10

Explanation of Items

(a) $798.11 additional depreciation has been allowed as a deduction in accordance with the decision of the United States Board of Tax Appeals, Docket No. 48615, Napa Valley Electric Company.

[fol. 58]

Schedule 11

Consolidated Net Income—1926

Net income as corrected:	
Great Western Power Company of California, Schedule (7)	$1,018,143.61
Napa Valley Electric Company, Schedule (9)	5,498.67
Consolidated net income	$1,023,642.28

Schedule 12

Computation of Total Tax for the Calendar Year ended December 31, 1926

			Net Income	Tax
Consolidated net income, Schedule (11)			$1,023,642.28	
Less: 1925 net loss under Section 206 of the 1926 Act.				
1925 net loss, Schedule (4)		($136,273.09)		
Less: Nontaxable income				
Dividends	$50.00			
Interest on U. S. obligations	2,087.21	2,137.21	134,135.88	
Taxable at 13½%			$889,506.40	$120,083.37

[fol. 59]

Schedule 13

Allocation of Corrected Tax

Name of Company	Net Income	Tax
Great Western Power Company of California	$884,007.73	$119,341.05
Napa Valley Electric Company	5,498.67	742.32*
Total	$889,506.40	$120,083.37

Schedule 14

Summary of Tax

Great Western Power Company of California

Correct tax Schedule (13)		$119,341.05
Tax previously assessed on consolidated return, Account # 402966	$140,138.86	
Less:		
Amount allocated to other companies	27,532.69	
Net amount assessed		112,606.17
Deficiency		$6,734.88

DGJ/NK

* The tax liability of the Napa Valley Electric Company has been previously determined by the United States Board of Tax Appeals under docket No. 48615.

[fol. 60] Transcript of Account

IT:AR:BTA-Recomp.
DGJ.

In re Great Western Power Company of California

San Francisco, California

B. T. A. Docket #48617

1924

Tax assessed on consolidated return filed by the Western Power Corporation:

Original, Account #405628		$136,611.47
Tax allocated to other companies as stipulated		22,125.00
Balance		$114,486.47
Tax paid:		
March 23, 1925	$33,000.00	
April 16, 1925	1,158.63	
June 15, 1925	34,152.87	
September 22, 1925	34,152.87	
December 16, 1925	34,152.86	
Total	136,617.23	
Less:		
Interest	5.76	
Tax paid	$136,611.47	

[fol. 61] Opinion

Less:		
Tax allocated to other companies	22,125.00	
Balance paid		114,486.47
Unpaid assessment to be abated		None
Tax paid		$114,486.47
Correct tax liability		28,396.91
Overpayment		$86,089.56

DGJ/NK.

BEFORE UNITED STATES BOARD OF TAX APPEALS

Docket No. 48617

GREAT WESTERN POWER COMPANY OF CALIFORNIA, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Promulgated April 26, 1934

1. Where a bond issue is retired before maturity by redemption of the bonds for cash, a taxpayer is entitled to a

deduction from income of the amount of unamortized discount and other financing costs in the year of such redemption and retirement.

[fol. 62] 2. A taxpayer is entitled to a deduction of an amount representing unamortized discount and other financing costs in the year of redemption and retirement of a bond issue before maturity, notwithstanding the fact that part of the bonds were redeemed for cash and part were exchanged for other bonds of a later issue.

Thomas R. Dempsey, Esq., for the Petitioner.
F. R. Shearer, Esq., for the Respondent.

Opinion

VAN FOSSAN:

This proceeding was brought to redetermine deficiencies in the income taxes of the petitioner for the years 1924, 1925, and 1926 in the amounts of $26,293.40, $187,883.90, and $133,333.99, respectively.

Several allegations of error were disposed of by stipulation, leaving for decision the following questions:

(1) The proper treatment of the sum of $248,363.02 claimed as a deduction from income for 1924, the item representing unamortized bond discount, expenses, and premiums paid in connection with a bond issue retired in 1924 before maturity, in part by payment of cash and in part by the exchange of the bonds for bonds of a later issue.

(2) The similar question as to a sum of $868,169.12 applicable to a second bond issue redeemed for cash and retired in 1925 before maturity.

The petitioner also asserts that the adjustments covered by stipulation and the second assigned error will result in [fol. 63] an operating loss which should be carried forward as a deduction in determining its net taxable income for the year 1926.

The facts were stipulated, and, so far as material to the issues, are substantially as follows:

1. At all times herein material the Great Western Power Company of California, hereinafter called the petitioner, was a public utility corporation engaged in the generation of electricity and its distribution in and about the cities of San Francisco, Oakland, Sacramento, and others in central

California. As a public utility the petitioner was subject to the jurisdiction of the California State Railroad Commission and kept its books on the accrual basis in accordance with the classification of accounts prescribed by the said commission. The petitioner's income tax returns for the years herein involved were made on the accrual basis.

2. On March 1, 1919, the petitioner executed a trust indenture entitled "First and Refunding Mortgage." Pursuant to the said indenture the petitioner has issued four series of its "First and Refunding Mortgage Sinking Fund Gold Bonds." The individual series of these bonds have been styled "Series A 6%," "Series B 7%," "Series C 6%," and "Series D 5½%" respectively, but hereinafter for the sake of brevity the various issues will be referred to merely as the "Series A 6's," "Series B 7's," etc. Likewise the indenture will hereinafter be referred to as the "Refunding Mortgage." All of the Series B and Series [fol. 64] D bonds which may be material to the present controversy were authorized as set forth in certain resolutions of the petitioner's board of directors dated December 7, 1920, April 8, 1921, June 21, 1921, February 5, 1925, February 5, 1925, May 15, 1925, and September 25, 1925.

3. On August 1, 1920, the petitioner executed a second trust indenture, hereinafter referred to as the "Mortgage Indenture."

4. During the year 1920 the petitioner, pursuant to the terms of the Mortgage Indenture, issued and sold $5,000,000 face value of its General Mortgage 8 per cent Gold Bonds dated August 1, 1920, and due August 1, 1930. These bonds, which will hereinafter be referred to as the "General Mortgage 8's," were, under the provisions of the Mortgage Indenture, convertible under certain conditions into Series B 7's and in 1922 the holders of $4,671,100 face value thereof actually made such conversion.

5. On February 1, 1921, the petitioner executed a third trust indenture, hereinafter referred to as the "General Lien Indenture."

6. During the year 1921 the petitioner, pursuant to the provisions of the General Lien Indenture, issued and sold $2,500,000 face value of its General Lien 8 per cent Gold Bonds dated February 1, 1921, and due February 1, 1936.

These bonds, which will hereinafter be referred to as the [fol. 65] "General Lien 8's," were sold at a discount of $150,000 and the expense of issuance was $22,283.54. The General Lien 8's were convertible under certain circumstances into Series B 7's, and on August 1, 1924, the holders of $2,354,500 face value thereof actually made such conversion.

7. Prior to December 31, 1923, the petitioner had purchased and retired $11,000 face value of the General Lien 8's and the unamortized discount and expense of issuance applicable thereto was charged off as a loss in the year of retirement.

8. On August 1, 1924, pursuant to a resolution adopted by the petitioner's board of directors on May 8, 1924, the holders of $2,354,500 face value of the General Lien 8's exchanged them for a like amount of Series B 7's and received, in addition to the Series B bonds, a cash premium of $117,725. Such exchange was made in accordance with the provisions of the option granted by the General Lien Indenture. The unamortized discount and expense applicable to such converted bonds was, on August 1, 1924, $126,176.97 and the expense of conversion was $1,461.05. The sum of the three items named: The premium paid, unamortized discount and expense of conversion, was $245,363.02, of which the respondent has allowed as a deduction for the year 1924 only $2,027.96 and for the year 1926 only $8,735.78.

[fol. 66] The petitioner contends that the full amount of $245,363.02 is allowable as a deduction for the year 1924, whereas the respondent contends that such amount should be amortized over the life of the Series B 7's which were exchanged for the General Lien 8's. If the $245,363.02 be allowed in full as a deduction for the year 1924, the petitioner's net income for the year 1926 as shown in the deficiency letter may be increased by the sum of $8,735.78.

9. As of August 1, 1924, the petitioner purchased for cash and retired all of the General Lien 8's which remained outstanding after the conversion referred to in paragraph 8. These outstanding bonds, which were of a face value of $134,500, were purchased by the petitioner at a premium of $6,725; the unamortized discount and expense applicable to such bonds on August 1, 1924, was $7,207.82 and the

expense of retirement was $83.46. The sum of the three items named: to wit, premium paid on retirement, unamortized discount and expense, and expense of retirement, is $14,016.28, of which the respondent has allowed as a deduction for 1924 only $5,464.08. The respondent now concedes that the balance of $8,552.20 is also an allowable deduction for the year 1924.

10. During the year 1921 the petitioner issued its second series of bonds under the refunding mortgage. These bonds, the Series B 7's, were dated August 1, 1920, and were due August 1, 1950.

[fol. 67] 11. The said Series B 7's were issued to a face value of $8,500,000 and were disposed of as follows:

Par value	Disposal
Par value	Disposal
$5,000,000	Delivered to the trustees under the General Mortgage Indenture and held by them as additional security for the General Mortgage 8's.
$2,500,000	Delivered to the trustees under the General Lien Indenture and held by them as additional security for the General Lien 8's.
$1,000,000	Sold to the public in 1921 for cash at a discount of $100,000.
$8,500,000	Total issued.

The expense of issuing the entire Series B was $49,548.14.

12. The $5,000,000 face value of Series B 7's delivered to the General Mortgage trustees were disposed of by them as follows: $4,671,100 face value were exchanged in 1922 for a like amount of General Mortgage 8's outstanding in the hands of the public and the remaining $328,900 were returned to the petitioner by reason of the cash redemption after the call date of a like amount of General Mortgage 8's. [fol. 68] None of the Series B 7's so returned to the petitioner were thereafter re-issued.

13. The $2,500,000 face value of Series B 7's delivered to the General Lien trustees were disposed of by them as follows: $2,354,500 were exchanged on August 1, 1924, for a like amount of General Lien 8's outstanding in the hands of the public and of the remainder, $145,500 face value,

$11,000 face value were returned to the petitioner by reason of the latter's retirement and delivery to the trustees for cancellation of a like amount of General Lien 8's which the petitioner had purchased from the public for cash, and $134,500 were returned to the petitioner by reason of the cash redemption after the call date of a like amount of General Lien 8's. None of the Series B 7's so returned to the petitioner were thereafter reissued. In addition to the $474,400 face value of Series B 7's which were reacquired by the petitioner as indicated above, $603,000 face value of the Series B 7's were reacquired by the petitioner prior to June, 1925, and as to such bonds there is no dispute.

14. In 1925 the petitioner began and consummated a program of partial refinancing which resulted in the retirement of its outstanding Series B 7's and the issuance of a fourth series of bonds under the "Refunding Mortgage." These new bonds, the Series B 5½'s were dated February 1, 1925, were due February 1, 1955, and bore interest at the rate [fol. 69] of 5½ per cent per annum. The following is a tabular analysis of the retirement of the Series B 7's:

Date	Par value of Bonds retired	Premiums Paid in cash	Unamortized Discount and expense	Expense of Retirement
June, 1925.....	$419,700.00	$43,415.22	$7,399.61	.....
July, 1925.....	257,400.00	10,863.50	4,523.15	.....
Aug. 1, 1925.....	6,745,500.00	674,550.00	117,989.72	.....
Totals.....	$7,422,600.00	$728,828.72	$129,912.48	$9,447.92

The following is a tabular analysis of the issuance of the Series D 5½'s:

Date	Purchaser	Par value	Discount	Expense of issuance
March, 1925.....	E. H. Rollins & Sons	$1,500,000	$112,506	$47,094.15
June 10, 1925.....	E. H. Rollins & Sons	6,300,000	315,000	
July 15, 1925.....	Western Power Corp.	700,000	35,000	
Subsequent to Aug. 1, 1925.....	E. H. Rollins & Sons	1,000,000	50,000	

All of the Series B 7's were redeemed for cash. The amounts necessary for the June, 1925, and July, 1925 redemptions and for the payment of the expense item of $9,447.92 were taken from the general funds in the petitioner's treasury. The amount of cash necessary for the

August 1, 1925, redemption was $7,420,500. This amount was derived from the following sources:

[fol. 70] By the previous issuance and sale of $7,000,000 face value of Series D 5½'s at a discount of 5%	$6,650,000
Petitioner's general funds (including $141,808.32 representing interest accrued on the $7,000,000 of bonds from February 1, 1925, to date of issuance)	770,050
	$7,420,050

The amounts of $6,650,000 and $141,808.32 indicated above as derived from the sale of Series D 5½'s were not received by the petitioner, but were paid by the purchasers to the Bank of America and held in escrow until August 1, 1925, and were then paid directly to the trustees under the "Refunding Mortgage."

During the year 1925 the Railroad Commission of California, pursuant to application filed by the petitioner, issued its opinions and orders dated February 5, 1925, May 27, 1925, and October 21, 1925, and numbered respectively 14541, 14979 and 15544, granting permission to the petitioner to issue and sell the several installments of Series D 5½ per cent refunding mortgage bonds.

15. The petitioner contends that the sum of $868,189.12 representing the items "Premiums Paid"—$728,828.72, "Unamortized Discount and Expense"—$129,912.48 and [fol. 71] "Expense of Retirement"—$9,447.92 shown above in connection with the retirement of the Series B 7's constitutes an allowable deduction for the year 1925.

The respondent contends (a) that said sum of $868,189.12 (including also the unamortized portion of the amounts referred to in paragraph (8) hereof) should be treated as part of the capital cost of refinancing and refunding the petitioner's bonded indebtedness, and should be treated in its entirety as applicable to the Series D 5½'s maturing February 1, 1955, and amortized over the remaining life of the Series D 5½'s; (b) that $\frac{\$7,000,000}{\$7,422,600}$ of said sum should be treated as applicable to the Series D 5½'s to be amortized over their remaining life; (c) that the sums of

$674,550, $117,989.72 $\frac{\$6,745,500}{\$7,422,500}$ of the expense of retirement and the unamortized portion of the amounts referred to in paragraph 8 hereof should be treated as applicable to the Series D 5½'s and amortized over their remaining life; or (d) that at least $\frac{\$6,650.000}{\$7,420,050}$ of the amount referred to in (c) should be treated as applicable to the Series D 5½'s and amortized over their remaining life.

16. In determining the deficiencies for the years 1924, 1925 and 1926 the respondent allowed deductions in respect [fol. 72] to the petitioner's General Lien 8's, Series B 7 and Series D 5½'s as indicated below:

Description	1924	1925	1926
General Lien 8's:			
Amortization of discount and expense on outstanding bonds	*$6,765.90	.....	.....
Loss on retirements	5,464.08 (See par. 9)	.....	.....
"B 7's" Account General Lien 8's:			
Amortization of premiums, discount and expense on General Lien 8's converted into Series B 7's on Aug. 1, 1924	2,027.96 (See par. 8)	.....	.....
Series B 7's:			
Amortization of discount and expense on outstanding bonds	*5,227.32	*$3,039.57	.....
Loss on bond retirements (Prior to June, 1925)	.....	*4,046.56	.....
"D 5½'s" Account Series B:			
Amortization of amounts referred to in par. 8 hereof	.....	.....	$8,735.78 (See par. 8)
Series D 5½'s:			
Amortization of discount and expense of issuance	.....	*9,047.44	*18,782.28
Loss on bond retirements prior to Dec. 31, 1925	.....	*3,714.34	.....

* There is no dispute between the parties with reference to these items.

[fol. 73] 17. In addition to the adjustments to the petitioner's tax liability which may result from the foregoing facts, the petitioner is entitled to the following deductions from the amounts of net income indicated in the notice of deficiency: [Here follows a list of deductions aggregating $26,558.76 for 1924 and $11,928.18 for 1926, to which it is agreed petitioner is entitled and which will be allowed in settlement under Rule 50.]

18. The amounts of unamortized discount and expense, premiums paid, and expense of retirement applicable to the General Lien 8's (referred to in paragaph 8 hereof) were not charged to profit and loss on the petitioner's books, but were transferred to "Discount and Expense Series B Account General Lien" to be amortized over the remaining life of the Series B 7's. The amounts of unamortized discount and expense (including the unamortized portion of the amounts referred to above), premiums paid, and expense of retirement applicable to the Series B 7's (referred to in paragraph 14 hereof) were not charged to profit and loss on the petitioner's books, but were transferred to "Discount and Expense Series D 5½'s Account Series B 7's" to be amortized over the remaining life of the Series D 5½'s.

19. In the event that it be determined that the petitioner sustained an operating loss for the calendar year 1925, the petitioner and respondent stipulated that for the purpose of computing the net loss under section 206 of the [fol. 74] Revenue Act of 1926 to be deducted from the petitioner's net income for the calendar year 1926, such operating loss should be adjusted on account of the following items:

Dividends of domestic corporations	$50.00
Non-taxable interest on obligations of the United States	2,087.21
Total adjustment	$2,137.21

Petitioner's position as to the premiums paid, unamortized discount and expenses attaching to the bonds retired for cash in 1925 is amply supported by the decisions of the Board and the courts. S. & L. Building Corp., 19 B. T. A. 788; East Ninth Euclid Co., 26 B. T. A. 32 (affirmed on rehearing, 27 B. T. A. 1289); Indiana Lamp Corp., 28 B. T. A. 491; National Tile Co., 30 B. T. A. ——, SanJoaquin Light & Power Co. v. McLaughlin, 65 Fed. (2d) 677; Union Pacific R. R. Co. v. Commissioner, — Fed. (2d) — (C. C. A., 2d Cir. Feb. 13, 1934). The deduction should have been allowed in 1925 when the bonds were redeemed and retired.

As to the year 1924 petitioner has been allowed previously, or respondent at the hearing has conceded the

propriety of, a deduction for all unamortized discount and expense attaching to bonds retired by the payment of cash. The only question remaining for solution is the treatment of similar items of premium paid, unrecovered discount, and expense attaching to the $2,354,500 General Lien 8's which were exchanged by the holders for a like number of Series B 7's, plus a cash premium.

[fol. 75] In 1921, petitioner issued $2,500,000 par value of General Lien 8's for the purpose of acquiring new capital. The discount and other selling expenses were incurred at that time and constituted a cost of acquiring such new capital. Such cost related solely to the issue of the $2,500,000 General Lien 8's and by accepted practice was amortizable over the life of the bonds. Western Maryland Ry. Co. v. Commissioner, 33 Fed. (2d) 695; Union Pacific R. R. Co. v. Commissioner, supra.

When in 1924 the General Lien 8's were reacquired and retired in part by payment of cash and in part by exchange of the outstanding General Lien 8's for Series B 7's, plus a cash premium, the process of amortization was interrupted. The Series B 7's issued August 1, 1920, were a part of a totally different bond issue, and though both were related to the First and Refunding Mortgage of 1919 in that they looked to that mortgage for security, they constituted wholly separate steps in petitioner's financing. Each issue had its own costs and was entitled to amortize such costs over the life of its bonds. Respondent conceded by his treatment of the same that the unrecovered costs attaching to the bonds of the General Lien 8's issue reacquired for cash constituted a deductible loss in 1924 when so purchased and retired. We can see no proper basis for distinguishing in principle the bonds retired after reacquisition by exchanging the Series B 7's plus a cash premium. The General Lien 8's bond issue was pro tanto wiped out and there were no longer any bonds to which the unrecovered costs were kin or to which they could adhere. These costs were not part of the cost of floating the Series [fol. 76] B 7's, nor were they related to the bonds of that series in any other way. In our opinion there was no such interissue relationship as to permit us to say that when part of the General Lien 8's were exchanged for a like number of Series B 7's the incidents of the General Lien 8's were separated therefrom and attached to the Series

B 7's. The General Lien 8's paid 8 per cent and matured in 1936. The Series B 7's paid 7 per cent and matured in 1950. Assuming a contrary holding, the query would at once arise as to the period over which the unrecovered costs should be spread. Should the same amount allowed as a proportionate annual deduction under the old issue be permitted until exhaustion, or would only a lesser amount proportioned to the entire term of the new issue be deductible? The answer which we have reached as to the major question obviates the necessity of considering this question and other practical obstacles consequent on a contrary decision.

We believe the matter is to be determined from the standpoint of the issuing corporation and its action in the premises rather than from the position of the bondholders and the fact that some of the bondholders chose to exercise their option and accept the new bonds and a cash premium in exchange for the old bonds. In other words, the case should be determined on the basis of principle rather than on the ground of circumstance. The Board and the courts have approved the deductibility of unrecovered costs in the instance of cash redemption and here the respondent concedes the same. We can not distinguish in principle the situation where, in the same transaction, part of the bondholders exchange their bonds for those of the new issue plus a cash premium.

[fol. 77] We need not consider a situation, if it could conceivably exist, in which a subsequent issue by its terms takes the place of a former issue, both being parts of a general plan, and the exchange being mandatory. Here the right to exchange was optional with the bondholders. As to whether an exercised right of conversion could have the effect of extending the term of bonds, see Bonwit Teller & Co. v. Commissioner, 53 Fed. (2d) 381; certiorari denied, 284 U. S. 690.

In an almost identical situation the Circuit Court of Appeals for the Ninth Circuit held, in San Joaquin Light & Power Co. v. McLaughlin, supra, that unrecovered costs attached to bonds which were redeemed in part in cash and in part by exchange for a new series were all deductible from income in the year of redemption. We are of the opinion that the premiums paid, unamortized discount, and other financing costs related to the bonds of the series Gen-

eral Lien 8's retired in 1924 were deductible in that year. Reviewed by the Board.

Decision will be entered under Rule 50.

DISSENTING OPINION

STERNHAGEN, dissenting:

In my opinion the proportionate unamortized discount and costs of the General Lien 8's, dealt with in the second point, should not be deducted in 1924 when they were converted, as originally provided, into 7's; but should be spread over the term of the 7's. I agree with Judge Mack's dissenting opinion in San Joaquin Light & Power Co. v. McLaughlin, 65 Fed. (2d) 677, that the obligation of the 7's should be regarded as a continuation pro tanto of the indebtedness of the original issue.

[fol. 78] BEFORE UNITED STATES BOARD OF TAX APPEALS

[Title omitted]

MOTION TO AMEND OPINION

Comes now the Petitioner in the above entitled case and by its counsel moves this Honorable Board to amend its opinion promulgated therein on April 26, 1934, by correcting the following typographical errors:

(a) Paragraph 3—(Designated in the opinion as question number 1): The figure $248,363.02 should be $245,363.02. See paragraph 2 of subdivision 8 of the stipulation of facts filed with the Board on September 19, 1933.

(b) Paragraph 4—(Designated in the opinion as question number 2): The figure $868,169.12 should be $868,189.12. See subdivision 15 of the stipulation of facts referred to above.

(c) Subdivision 14 of the stipulated facts set forth in the opinion, second sentence: This sentence now reads, "These new bonds, the Series B 5½'s etc." The sentence should

read, "These new bonds, the Series D 5½'s etc." See [fol. 79] subdivision 14 of the stipulation of facts referred to above.

(d) Subdivision 17 of the stipulated facts set forth in the opinion, sentence in brackets: This sentence should be changed to read, "Here follows a list of deductions aggregating $1,220.00 for 1924, $26,558.76 for 1925, and $11,928.18 for 1926, which it is agreed etc." See subdivision 17 of the stipulation of facts referred to above.

Thomas R. Dempsey, A. Calder Mackay, Attorneys for Petitioner, 1104 Pacific Mutual Bldg., Los Angeles, California.

BEFORE UNITED STATES BOARD OF TAX APPEALS

Docket No. 48617

GREAT WESTERN POWER COMPANY OF CALIFORNIA, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

DECISION

Pursuant to the Opinion of the Board promulgated April 26, 1934, the respondent herein on June 6, 1934, filed a notice of settlement and proposed computation, and the [fol. 80] petitioner on June 9, 1934, having filed counter proposed computation and notice of settlement, and on June 19, 1934, having also filed an acquiescence to respondent's proposed computation, now therefore, it is

Ordered and decided that there is an overpayment in income tax of $86,089.56 for the year 1924; that there is no deficiency for the year 1925; and that there is a deficiency of $6,734.88 for the year 1926.

(S.) C. M. Trammell, Member.

Entered June 26, 1934.

IN UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

[Title omitted]

PETITION FOR REVIEW AND ASSIGNMENTS OF ERROR

To the Honorable Judges of the United States Circuit Court of Appeals for the Second Circuit:

Now comes Robert H. Jackson, Commissioner of Internal [fol. 81] Revenue, by his attorneys, Frank J. Wideman, Assistant Attorney General, Robert H. Jackson, Assistant General Counsel for the Bureau of Internal Revenue, and Paul E. Waring, Special Attorney, Bureau of Internal Revenue, and respectfully shows:

I

Jurisdiction

The petitioner on review (hereinafter referred to as the Commissioner) is the duly appointed, qualified and acting Commissioner of Internal Revenue of the United States, holding his office by virtue of the laws of the United States. The respondent on review (hereinafter referred to as the taxpayer) is a corporation existing under and by virtue of the laws of California, with its principal place of business at 530 Bush Street, San Francisco, California. The information income tax return of the taxpayer for the calendar year 1924, being the period involved herein, was filed with the Collector of Internal Revenue for the First District of California at San Francisco, California; that the taxpayer during the year 1924 was a subsidiary of the Western Power Corporation and joined with that company in filing a consolidated return; that the principal place of business of said Western Power Corporation is 25 Broad Street, New York City, New York, and that the said consolidated return was filed with the Collector of Internal Revenue at New York City, New York; and that the office of said Collector is located within the jurisdiction of the said Circuit Court of Appeals for the Second Circuit.

[fol. 82] For the years 1925 and 1926, taxpayer filed its consolidated income tax returns with the Collector of Internal Revenue at San Francisco, California, which office

of the Collector is within the jurisdiction of the Ninth Circuit Court of Appeals. The question of venue for appeal is controlled by Section 1002 of the Revenue Act of 1926, as amended by Section 519 of the Revenue Act of 1934; and therefore, the entire decision of the Board entered June 26, 1934, which relates to the years 1924, 1925 and 1926, in respect of which the liability arises, may be reviewed by the Circuit Court of Appeals for the Second Circuit.

The Commissioner of Internal Revenue determined a deficiency in income taxes against the taxpayer for the calendar year 1924 of $26,293.40, for the calendar year 1925 of $187,883.90 and for the calendar year 1926 of $133,333.99; and on March 4, 1930, sent to it by registered mail a notice of said deficiency in accordance with the provisions of Section 274 of the Revenue Act of 1924, and Section 272 of the Revenue Act of 1926. Thereafter, on May 2, 1930, taxpayer filed an appeal from said notice of deficiency with the United States Board of Tax Appeals.

On September 19, 1933, the case was submitted to the Board of Tax Appeals at Washington, D. C., for its decision on an agreed statement of facts. The Board under date of April 26, 1934, promulgated its opinion, and on June 26, 1934, entered its decision and order of redetermination in accordance with the opinion wherein and whereby it ordered and decided that for the year 1924 there is an over-[fol. 83] payment in income tax of $86,089.56; that for the year 1925 there is no deficiency, and that for the year 1926 there is a deficiency of $6,734.88.

II

Nature of Controversy

The controversy herein grows out of and arises from the following:

The Great Western Power Company of California was a public utility corporation engaged in the generation of electricity and distribution thereof. As a public utility, the taxpayer was subject to the jurisdiction of the California State Railroad Commission and kept its books on the accrual basis in accordance with the classification of

accounts prescribed by the said Commission. Taxpayer's income tax returns for the years 1924, 1925 and 1926 were made on the accrual basis.

On March 1, 1919, the taxpayer executed a trust indenture entitled "First and Refunding Mortgage." Pursuant to said indenture, taxpayer has issued four series of its "First and Refunding Mortgage Sinking Fund Gold Bonds." The individual series of these bonds have been styled "Series A 6%," "Series B 7%," "Series C 6%," and "Series D 5½%," respectively, but hereinafter the various issues will be referred to merely as the "Series A 6's," "Series B 7's," etc. Likewise, the indenture hereinafter will be referred to as the "Refunding Mortgage." All of the Series B and Series D bonds, which may be material to the present controversy, were authorized as set forth in certain resolutions of the taxpayer's board of [fol. 84] directors, dated December 7, 1920, April 8, 1921, June 21, 1921, February 5, 1925, May 15, 1925 and September 25, 1925.

On August 1, 1920, the taxpayer executed a second trust indenture, hereinafter referred to as the "Mortgage Indenture."

During the year 1920 taxpayer, pursuant to the terms of the Mortgage Indenture, issued and sold $5,000,000.00 face value of its General Mortgage 8% Gold Bonds, dated August 1, 1920, and due August 1, 1930. These bonds, which will hereinafter be referred to as the "General Mortgage 8's," were, under the provisions of the Mortgage Indenture, convertible under certain conditions into the Series B 7's, and in 1922 the holders of $4,671,000.00 face value thereof actually made such conversion.

On February 1, 1921, taxpayer executed a third trust indenture, hereinafter referred to as the "General Lien Indenture."

During the year 1921 taxpayer, pursuant to the provisions of the General Lien Indenture, issued and sold $2,500,000.00 face value of its General Lien 8% Gold Bonds, dated February 1, 1921, and due February 1, 1936. These bonds, which will hereinafter be referred to as the "General Lien 8's," were sold at a discount of $150,000.00 and the expense of issuance was $22,283.54. The General Lien 8's were convertible under certain circumstances into Series B 7's, and on August 1, 1924, the holders of $2,-

354,500.00 face value thereof actually made such conversion.

Prior to December 31, 1923, the taxpayer purchased and retired $11,000.00 face value of the General Lien 8's and [fol. 85] the unamortized discount and expense of issuance applicable thereto was charged off as a loss in the year of retirement.

On August 1, 1924, pursuant to a resolution adopted by the taxpayer's board of directors on May 8, 1924, the holders of $2,354,500.00 face value of General Lien 8's exchanged them for a like amount of Series B 7's and received in addition to such Series B bonds, a cash premium of $117,725.00. Such exchange was made in accordance with the provisions of the option granted by the General Lien Indenture. The unamortized discount and expense applicable to such converted bonds was, on August 1, 1924, $126,176.97 and the expense of conversion was $1,461.05. The sum of the three items named: The premium paid, unamortized discount and expense of conversion, was $243,363.02, of which the Commissioner has allowed as a deduction for the year 1924 only $2,027.96, and for the year 1926 only $8,735.78.

The taxpayer contends that the full amount of $245,363.02 is allowable as a deduction for the year 1924, whereas the Commissioner contends that such amount should be amortized over the life of the Series B 7's which were exchanged for the General Lien 8's.

As of August 1, 1924, the taxpayer purchased for cash and retired all of the General Lien 8's which remained outstanding after the conversion. These outstanding bonds, which were of a face value of $134,500.00, were purchased by the taxpayer at a premium of $6,725.00; the unamortized discount and expense applicable to such bonds on August 1, 1924, was $7,207.82 and the expense of retire-
[fol. 86] ment was $83.46. The sum of the three items represent allowable deductions for the year 1924.

During the year 1921, the taxpayer issued its second series of bonds under the Refunding Mortgage. These bonds, the Series B 7's, were dated August 1, 1920, and were due August 1, 1950.

The said Series B 7's were issued to a face value of $8,500,000.00 and were disposed of as follows:

Par value	Disposal
$5,000,000.00	Delivered to the trustees under the General Mortgage Indenture and held by them as additional security for the General Mortgage 8's.
$2,500,000.00	Delivered to the trustees under the General Lien Indenture and held by them as additional security for the General Lien 8's.
$1,000,000.00	Sold to the public in 1921 for cash at a discount of $100,000.00.
$8,500,000.00	Total issued.

The expense of issuing the entire Series B was $49,548.14.

The $5,000,000.00 face value of Series B 7's delivered to the General Mortgage trustees were disposed of by them as follows: $4,671,100.00 face value were exchanged in 1922 for a like amount of General Mortgage 8's outstanding in the hands of the public, and the remaining $328,- [fol. 87] 900.00 were returned to the taxpayer by reason of the cash redemption after the call date of a like amount of General Mortgage 8's. None of the Series B 7's so returned to the taxpayer was thereafter re-issued.

The $2,500,000.00 face value of Series B 7's delivered to the General Lien trustees were disposed of by them as follows: $2,354,500.00 were exchanged on August 1, 1924, for a like amount of General Lien 8's outstanding in the hands of the public and of the remainder, $145,500.00 face value, $11,000.00 face value were returned to the taxpayer by reason of the latter's retirement and delivery to the trustees for cancellation of a like amount of General Lien 8's which the taxpayer had purchased from the public for cash, and $134,500.00 were returned to the taxpayer by reason of the cash redemption after the call date of a like amount of General Lien 8's. None of the Series B 7's so returned to the taxpayer were thereafter re-issued. In addition to the $474,400.00 face value of Series B 7's which were re-acquired by the taxpayer as indicated above, $603,000.00 face value of the Series B 7's were re-acquired by the taxpayer prior to June, 1925, and as to such bonds there is no dispute.

In 1925, the taxpayer began and consummated a program of partial refinancing which resulted in the retirement of its outstanding Series B 7's and the issuance of a

fourth series of bonds under the "Refunding Mortgage." These new bonds, the Series B 5½'s were dated February 1, 1925, were due February 1, 1955, and bore interest at the rate of 5½ per cent per annum. The following is a [fol. 88] tabular analysis of the retirement of the Series B 7's:

Date	Par value of Bonds retired	Premiums Paid in cash	Unamortized Discount and expense	Expense of Retirement
June, 1925.....	$419,700.00	$43,415.22	$7,399.61	.....
July, 1925.....	257,400.00	10,863.50	4,523.15	.....
Aug. 1, 1925.....	6,745,500.00	674,550.00	117,989.72	.....
Totals.....	$7,422,600.00	$728,828.72	$129,912.48	$9,447.92

The following is a tabular analysis of the issuance of the Series D 5½'s:

Date	Purchaser	Par value	Discount	Expense of issuance
March 1925.....	E. H. Rollins & Sons	$1,500,000	$112,500	
June 10, 1925.....	E. H. Rollins & Sons	6,300,000	315,000	
July 15, 1925.....	Western Power Corp.	700,000	35,000	$47,094.15
Subsequent to Aug. 1, 1925.....	E. H. Rollins & Sons	1,000,000	50,000	

All of the Series B 7's were redeemed for cash. The amounts necessary for the June, 1925, and July, 1925, redemptions and for the payment of the expense item of $9,447.92 were taken from the general funds in the taxpayer's treasury. The amount of cash necessary for the August 1, 1925, redemption was $7,420,500.00. This amount was derived from the following sources:

[fol. 89] By the previous issuance and sale of $7,000,000 face value of Series D 5½'s at a discount of 5% $6,650,000

Taxpayer's general funds (including $141,808.32 representing interest accrued on the $7,000,000 of bonds from February 1, 1925, to date of issuance) 770,050

$7,420,050

The amounts of $6,650,000.00 and $141,808.32 indicated above as derived from the sale of Series D 5½'s were not received by the taxpayer, but were paid by the purchasers to the Bank of America and held in escrow until August

1, 1925, and were then paid directly to the trustees under the "Refunding Mortgage."

During the year 1925, the Railroad Commission of California, pursuant to application filed by the taxpayer, issued its opinions and orders dated February 5, 1925, May 27, 1925, and October 21, 1925, and numbered respectively 14541, 14979 and 15544, granting permission to the taxpayer to issue and sell the several installments of Series D 5½ per cent refunding mortgage bonds.

Taxpayer contends that the sum of $868,189.12 representing the items "Premiums Paid"—$728,828.72, "Unamortized Discount and Expense"—$129,912.48 and "Expense of Retirement"—$9,447.92 shown above in connection with the retirement of the Series B 7's constitutes an [fol. 90] allowable deduction for the year 1925.

The Commissioner contends (a) that said sum of $868,189.12 (including also the unamortized portion of the amounts) should be treated as part of the capital cost of refinancing and refunding the taxpayer's bonded indebtedness, and should be treated in its entirety as applicable to the Series D 5½'s maturing February 1, 1955, and amortized over the remaining life of the Series D 5½'s; (b) that $\frac{\$7,000,000.00}{\$7,422,600.00}$ of said sum should be treated as applicable to the Series D 5½'s to be amortized over their remaining life; (c) that the sums of $674,550.00, $117,989.72, $\frac{\$6,745,500.00}{\$7,422,500.00}$ of the expense of retirement and the unamortized portion of the amounts should be treated as applicable to the Series D 5½'s and amortized over their remaining life; or (d) that at least $\frac{\$6,650,000.00}{\$7,420,050.00}$ of the amount referred to in (c) should be treated as applicable to the Series D 5½'s and amortized over their remaining life.

In determining the deficiencies for the years 1924, 1925 and 1926, the Commissioner allowed deductions in respect to the taxpayer's General Lien 8's, Series B 7's and Series D 5½'s, as indicated below:

[fol. 91]

Description	1924	1925	1926
General Lien 8's:			
Amortization of discount and expense on outstanding bonds	*$6,765.90	.....	.....
Loss on retirements	5,464.02	.....	.....
"B 7's" Account General Lien 8's:			
Amortization of premiums, discount and expense on General Lien 8's converted into Series B 7's on Aug. 1, 1924	2,027.96	.....	.....
Series B 7's:			
Amortization of discount and expense on outstanding bonds	*5,227.32	*$3,039.57	.....
Loss on bond retirements (Prior to June, 1925)	.....	*4,046.56	.....
"D 5½'s" Account Series B:			
Amortization of amounts	.....	.....	$8,735.78
Series D 5½'s:			
Amortization of discount and expenses of issuance	.....	*9,047.44	*18,782.28
Loss on bond retirements prior to Dec. 31, 1925	.....	*3,714.34	.....

* There is no dispute between the parties with reference to these items.

[fol. 92] The amounts of unamortized discount and expense, premiums paid, and expense of retirement applicable to the General Lien 8's were not charged to profit and loss on the taxpayer's books, but were transferred to "Discount and Expense Series B Account General Lien" to be amortized over the remaining life of the Series B 7's. The amounts of unamortized discount and expense (including the unamortized portion of the amounts referred to above), premiums paid, and expense of retirement applicable to the Series B 7's were not charged to profit and loss on the taxpayer's books, but were transferred to "Discount and Expense Series D 5½'s Account Series B 7's" to be amortized over the remaining life of the Series D 5½'s.

That as a result of and arising out of the pleadings and issues made and joined by the parties hereto before the United States Board of Tax Appeals, the following questions arose, and were presented to the Board:

(1) Whether the sum of $245,363.02, representing premiums, unamortized discount and expenses pertaining to $2,354,500.00 face amount of the taxpayer's General Lien 8% bonds converted on August 1, 1924, at the option of the bondholders, into a like face amount of taxpayer's Series B 7% bonds, should be deducted in its entirety in the year 1924; or whether said amount should in the first

instance be spread over the period from August 1, 1924 to August 1, 1950, the maturity date of the B 7's.

[fol. 93] (2) Whether the sum of $868,189.12, representing premiums, unamortized discount, and expenses pertaining to $7,422,600.00 face amount of the taxpayer's Series B 7% bonds retired in 1925, pursuant to a refinancing program, should be deducted in its entirety in the year 1925; or whether said sum (together with the unamortized portion of the amount referred to in Question [1]) should be spread over the period ending February 1, 1955, the maturity date of the taxpayer's Series D 5½% bonds issued in 1925.

(3) Whether the taxpayer sustained an operating loss for the year 1925 which should be carried forward as a deduction in determining its net taxable income for the year 1926.

A division of the Board of Tax Appeals held (1) that the amount mentioned in Question (1) should be deducted in the year 1924; (2) that the amount mentioned in Question (2) should be deducted in the year 1925, and (3) that as a result of such holdings (1) and (2) a net loss for the year 1925 resulted, which should be carried forward to reduce the taxpayer's taxable income for the year 1926.

III

Assignments of Error

The Commissioner says that in the record and proceeding before the Board of Tax Appeals and in the decision and final order of redetermination rendered and entered by the Board of Tax Appeals manifest errors occurred and [fol. 94] intervened to the prejudice of the Commissioner, and the Commissioner assigns the following errors and each of them which he avers occurred in said record, proceeding, decision and final order of redetermination, and upon which he relies to reverse the said decision and final order of redetermination so rendered and entered by the Board of Tax Appeals, to-wit:

(1) The Board erred in holding that the taxpayer was entitled to deduct from its gross income for the year 1924 the sum of $245,363.02, representing premiums, unamor-

tized discount and expenses pertaining to $2,354,500.00 face amount of taxpayer's general lien 8% bonds converted on August 1, 1924, at the option of the bondholders into a like face amount of taxpayer's Series B 7% bonds, there being no evidence to support this finding.

(2) The Board erred in holding that the taxpayer was entitled to deduct from its gross income for the year 1924 the amount of premiums pertaining to said general lien 8% bonds, there being no evidence to support this finding.

(3) The Board erred in holding that the taxpayer was entitled to deduct from its gross income for the year 1924 the amount of unamortized discount pertaining to said general lien 8% bonds, there being no evidence to support this finding.

(4) The Board erred in holding that the taxpayer was entitled to deduct from its gross income for the year 1924 [fol. 95] the expenses pertaining to said general lien 8% bonds, there being no evidence to support this finding.

(5) The Board erred in not holding that the sum of $245,363.02, representing premiums, unamortized discount and expenses pertaining to said general lien 7% bonds, should, in the first instance, be spread over the period from August 1, 1924 to August 1, 1950, the maturity days of the Series B 7% bonds, there being no evidence to support this finding.

(6) The Board erred in holding that the taxpayer was entitled to deduct from its gross income for the year 1925 the sum of $868,189.12, representing premiums, unamortized discount and expenses pertaining to $7,422,600.00 face amount of taxpayer's Series B 7% bonds retired in 1925, pursuant to a refinancing program, there being no evidence to support this finding.

(7) The Board erred in holding that the taxpayer was entitled to deduct from its gross income for the year 1925 the amount of premiums pertaining to said Series B 7%, there being no evidence to support this finding.

(8) The Board erred in holding that the taxpayer was entitled to deduct from its gross income for the year 1925 the unamortized discount pertaining to said Series B 7% bonds, there being no evidence to support this finding.

(9) The Board erred in holding that the taxpayer was entitled to deduct from its gross income for the year 1925 [fol. 96] the expenses pertaining to said Series B 7% bonds, there being no evidence to support this finding.

(10) The Board erred in not holding that the sum of $868,189.12, representing premiums, unamortized discount and expenses pertaining to said Series B 7% bonds, should be spread over the period ending February 1, 1955, the maturity date of taxpayer's Series D 5½% bonds issued in 1925, there being no evidence to support this finding.

(11) The Board erred in holding that the taxpayer was entitled to deduct from its gross income for the year 1926 the net loss as determined by it for the year 1925, there being no evidence to support this finding.

(12) The Board erred in entering an order and decision "That there is an overpayment in income tax of $86,089.56 for the year 1924; that there is no deficiency for the year 1925; and that there is a deficiency of $6,734.88 for the year 1926", there being no evidence to support this finding.

Wherefore, the Commissioner petitions that the decision of the Board of Tax Appeals be reviewed by the United States Circuit Court of Appeals for the Second Circuit, that a transcript of the record be prepared in accordance with law and with the rules of said Court and transmitted to the clerk of said Court for filing, and that appropriate action be taken to the end that the errors complained of [fol. 97] may be reviewed and corrected by said Court.

(Sgd.) Frank J. Wideman, Assistant Attorney General. (Signed) Robert H. Jackson, Assistant General Counsel for the Bureau of Internal Revenue.

Of Counsel: Paul E. Waring, Special Attorney, Bureau of Internal Revenue.

Duly sworn to by Paul E. Waring. Jurat omitted in printing.

[fol. 98] IN UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

[Title omitted]

NOTICE OF FILING PETITION FOR REVIEW

To Great Western Power Company of California, 530 Bush Street, San Francisco, California:

You are hereby notified that the Commissioner of Internal Revenue did, on the 13th day of September 1934, file with the Clerk of the United States Board of Tax Appeals, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Second Circuit, of the decision of the Board heretofore rendered in the above-entitled case. A copy of the petition for review and the assignments of error as filed is hereto attached and served upon you.

Dated this 14th day of September, 1934.

(Signed) Robert H. Jackson, Assistant General Counsel for the Bureau of Internal Revenue.

[fol. 99] Personal service of the above and foregoing notice, together with a copy of the petition for review and assignments of error mentioned therein, is hereby acknowledged this 18th day of September, 1934.

Great Western Power Company of California, Respondent on Review, by Ira Foote, Secretary-Treasurer.

IN UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

[Title omitted]

NOTICE OF FILING PETITION FOR REVIEW

To Thomas R. Dempsey, Esq., 1104 Pacific Mutual Building, Los Angeles, California:

You are hereby notified that the Commissioner of Internal Revenue did, on the 13th day of September, 1934, file [fol. 100] with the Clerk of the United States Board of Tax

Appeals, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Second Circuit, of the decision of the Board heretofore rendered in the above-entitled case. A copy of the petition for review and the assignments of error as filed is hereto attached and served upon you.

Dated this 14th day of September, 1934.

(Signed) Robert H. Jackson, Assistant General Counsel for the Bureau of Internal Revenue.

Personal service of the above and foregoing notice, together with a copy of the petition for review and assignments of error mentioned therein, is hereby acknowledged this 20th day of September, 1934.

(Sgd.) Thomas R. Dempsey, A. Calder Mackay, Attorney- for Respondent on Review.

[fol. 101] IN UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

[Title omitted]

MOTION TO CORRECT RECORD

Comes now Guy T. Helvering, Commissioner of Internal Revenue, and, appearing herein by his counsel of record, advises the Court that on the 14th day of September, 1934, there was filed in his behalf a petition for review by this Court of the cause entitled as in the caption hereof; which petition for review was filed on the day aforesaid with the Clerk of the United States Board of Tax Appeals, Washington, D. C., and copies of the said petition have heretofore been duly served upon the respondent therein named and upon counsel for the respondent.

That in said petition there occurred a clerical error in the first paragraph thereof in that such paragraph reads:

"Now comes Robert H. Jackson, Commissioner of In-
[fol. 102] ternal Revenue, by his attorneys, Frank J. Wideman, Assistant Attorney General, Robert H. Jackson, Assistant General Counsel for the Bureau of Internal Revenue, and Paul E. Waring, Special Attorney, Bureau of Internal Revenue, and respectfully shows:"

Whereas, as is manifest, it was intended and designed by the drafters of said petition for review that said paragraph read, and said paragraph should read, as follows:

"Now comes Guy T. Helvering, Commissioner of Internal Revenue, by his attorneys, Frank J. Wideman, Assistant Attorney General, Robert H. Jackson, Assistant General Counsel for the Bureau of Internal Revenue, and Paul E. Waring, Special Attorney, Bureau of Internal Revenue, and respectfully shows:"

Wherefore, counsel for petitioner on review moves this Honorable Court to pass an order correcting the record herein so that it will appear of record in the first paragraph of said petition for review as hereinabove last set forth; and that petitioner on review be directed to file a copy of said order with the Clerk of the United States Board of Tax Appeals to the end that said order shall be incorporated in the transcript of record.

(Sgd.) Frank J. Wideman, Assistant Attorney General. (Sgd.) Robert H. Jackson, Assistant General Counsel for the Bureau of Internal Revenue.

[fol. 103] Respondent consents to the granting of an order correcting the record as moved herein.

Dempsey & Mackay, (Sgd.) A. Calder Mackay.

IN UNITED STATES CIRCUIT COURT OF APPEALS, FOR THE SECOND CIRCUIT

[Title omitted]

ORDER GRANTING MOTION TO CORRECT RECORD

Upon consideration of the motion filed herein by the petitioner on review praying that this Court pass an order to correct a clerical error in the first paragraph of the petition for review filed with the United States Board of Tax Appeals on the 14th day of September, 1934,

It is by the Court this 10th day of Oct., 1934,

[fol. 104] Ordered that the said motion be and it is hereby granted, and the petitioner on review is directed to incorporate a copy of said motion and this order in the transcript

of record on review in said cause to be certified to this Court in due course.

Manton, Justice.

Filed Oct. 10, 1934. A true copy. (Sgd.) Wm. Parkin, Clerk.

In United States Circuit Court of Appeals for the Second Circuit

B. T. A. No. 48617

Guy T. Helvering, Commissioner of Internal Revenue, Petitioner,

v.

Great Western Power Company of California, Respondent

Statement of the Evidence

The following is a statement in narrative form of the evidence in the above-entitled proceeding. The proceeding [fol. 105] came on for hearing pursuant to notice on September 19, 1933, at San Francisco, California, before the Honorable Ernest H. Van Fossan, Member of the United States Board of Tax Appeals, whereupon the following proceedings were had, and evidence heard and received:

Thomas R. Dempsey, Esq., appeared on behalf of the Great Western Power Company of California (hereinafter sometimes referred to as "taxpayer").

F. R. Shearer, Esq. (E. Barrett Prettyman, General Counsel, Bureau of Internal Revenue) appeared on behalf of the Commissioner of Internal Revenue (hereinafter referred to as "Commissioner").

On motion of counsel for the taxpayer, leave was granted to amend the taxpayer's petition, whereupon the First Amended Petition was filed, and a copy thereof served on counsel for the Commissioner. Thereupon, counsel for the Commissioner filed his Answer to First Amended Petition, a copy of which was duly served on counsel for the taxpayer.

Counsel for the parties had theretofore, on June 5, 1933, filed with the Board of Tax Appeals a duly signed Stipula-

tion of Facts. This Stipulation of Facts was duly brought to the attention of the presiding member and (omitting the caption and the signatures) is in words and figures as follows:

STIPULATION OF FACTS

It is hereby stipulated and agreed by and between the parties hereto as follows:

[fol. 106] 1. For the calendar year 1924 the petitioner's reported income was included in a consolidated return in the name of Western Power Corporation, 25 Broad Street, New York, N. Y., and affiliated companies. The Commissioner held that petitioner was not affiliated with any other corporation during the year 1924, and determined the deficiency on the basis of its separate income. The amount shown as the tax and assessed and paid on the basis of said consolidated return was $136,611.47 and appears on Account #405628, April, 1925. By agreement dated June 5, 1931, between the interested corporations the tax so computed and paid on the consolidated return was allocated as follows:

To the California Electric Generating Company (appeal pending under Docket No. 48616)	$ 22,125.00
To the petitioner, Great Western Power Company of California	114,486.47
Total	$136,611.47

In Docket No. 48616 the parties have entered into a stipulation for the redetermination of the tax liability of California Electric Generating Company for the year 1924 based upon this allocation. In the redetermination of petitioner's tax liability for the year 1924 this same allocation of tax previously assessed and paid shall be adhered to.

2. For the calendar year 1925 the petitioner and the California Electric Generating Company joined in a consolidated return. The Commissioner determined that the peti- [fol. 107] tioner was not affiliated with any other corporation during the year 1925 and determined the deficiency on the basis of its separate income. The amount shown as the tax and assessed and paid on the basis of said consoli-

dated return was $5,088.10 and appears on Account #400600, September, 1926. The entire amount thereof is properly allocable to the California Electric Generating Company. In Docket No. 48616 the parties have entered into a stipulation for the redetermination of the tax liability of the California Electric Generating Company for the year 1925 in accordance therewith.

3. For the calendar year 1926 the petitioner joined in a consolidated return with the California Electric Generating Company and the Napa Valley Electric Company. The Commissioner held that petitioner was not affiliated with the California Electric Generating Company during the year 1926 and determined the deficiency on the basis of the consolidated income of the petitioner and the Napa Valley Electric Company. The amount shown as the tax and assessed and paid on the basis of said consolidated return was $140,138.86, and appears on Account #402966, May, 1927. This amount is properly allocable as follows:

To the California Electric Generating Company	$ 27,532.69
To the Napa Valley Electric Company	None.
To the petitioner, Great Western Power Company of California	112,606.17
Total	$140,138.86

[fol. 108] In Docket Nos. 48615 and 48616, the parties have entered into stipulations for the redetermination of the tax liability of the Napa Valley Electric Company and the California Electric Generating Company for the year 1926 based on this allocation. In the redetermination of petitioner's tax liability for the year 1926, this same allocation shall be adhered to.

4. As determined by the Commissioner the Napa Valley Electric Company's portion of the consolidated net income for the year 1926 was $6,296.78. In determining that amount the Commissioner allowed depreciation in the amount of $5,128.80. The amount of depreciation allowable is $5,926.91, or $798.11 in excess of that allowed by the Commissioner. Accordingly, the correct amount of the income of Napa Valley Electric Company to be included in the consolidated net income of petitioner and said com-

pany for the year 1926 is $5,498.67. Of the correct consolidated tax liability (as hereinafter determined in this proceeding) the amount of $742.32 is allocable and shall be allocated to the Napa Valley Electric Company. In Docket No. 48615 the parties have entered into a stipulation for the redetermination of the tax liability of the Napa Valley Electric Company for the year 1926 in accordance with the above depreciation adjustment and the above allocation.

5. Petitioner accepts the Commissioner's determination in respect of affiliation and non-affiliation for the years 1924, 1925 and 1926, and waives and withdraws the issue with [fol. 109] respect to consolidating the income and/or accounts of the petitioner with those of other corporations, as set forth in sub-paragraph 4 of paragraph IV of the petition in this proceeding.

6. The following tabulation is a correct statement showing the amounts of depreciation sustained by the petitioner on depreciable assets used in its trade or business during the calendar years 1924, 1925 and 1926, the amounts of depreciation allowed by the Commissioner in determining petitioner's income for 1924 and 1925 and petitioner's portion of the consolidated income for 1926, and the amounts of additional deductions for depreciation to be allowed in recomputing petitioner's income for 1924 and 1925 and petitioner's portion of the consolidated income for 1926:

Year	Depreciation sustained	Depreciation allowed by commissioner	Addl. deductions for depreciation to be allowed
1924	$1,152,571.00	$528,017.63	$624,553.37
1925	1,234,772.00	547,986.04	686,785.96
1926	1,378,690.00	578,247.07	800,442.93

This paragraph disposes of the issue with respect to the alleged failure of the Commissioner to allow as deductions reasonable sums for exhaustion, wear and tear and obsolescence as set forth in sub-paragraph 1 of paragraph IV, and sub-paragraph (d) of paragraph V of the petition in this proceeding.

[fol. 110] 7. The parties hereto reserve the right to introduce at the hearing before the Board competent and material evidence relevant to any issue presented by the

pleadings, as they now exist or may be amended, except the issues disposed of and waived by this stipulation.

Thereupon, counsel for the parties offered a further stipulation of facts which was duly received in evidence as Stipulation of Facts No. 2, and (omitting the caption and signature) is in words and figures as follows:

STIPULATION OF FACTS No. 2

It is hereby stipulated and agreed by and between the parties hereto, by their respective counsel of record that:

(1) At all times herein material the Great Western Power Company of California, hereinafter called the Petitioner, was a public utility corporation engaged in the generation of electricity and its distribution in and about the cities of San Francisco, Oakland, Sacramento, and others in Central California. Being a public utility Petitioner was subject to the jurisdiction of the California State Railroad Commission and kept its books on the accrual basis in accordance with the classification of accounts prescribed by said Commission. Petitioner's income tax returns for the years herein involved were made on the accrual basis.

(2) On March 1, 1919, Petitioner executed a trust indenture entitled "First and Refunding Mortgage." Pur- [fol. 111] suant to said indenture, a copy of which is attached hereto and marked Exhibit "A," Petitioner has issued four series of its "First and Refunding Mortgage Sinking Fund Gold Bonds." The individual series of these bonds have been styled "Series A 6%," "Series B 7%," "Series C 6%," and "Series D 5½%" respectively, but hereinafter for the sake of brevity the various issues will be referred to merely as the "Series A 6's," "Series B 7's," etc. Likewise the indenture will hereinafter be referred to simply as the "Refunding Mortgage." All of the Series B and Series D bonds which may be material to the present controversy were authorized as set forth in certain resolutions of Petitioner's Board of Directors dated Dec. 7, 1920, April 8, 1921, June 21, 1921, February 5, 1925, February 5, 1925, May 15, 1925, and September 25, 1925, copies of which are attached hereto as Exhibits A1, A2, A3, A4, H, I and J, respectively.

(3) On August 1, 1920, Petitioner executed a second trust indenture which will hereinafter be referred to as the "Mortgage Indenture."

(4) During the year 1920 Petitioner, pursuant to the terms of the Mortgage Indenture, issued and sold $5,000,000.00 face value of its General Mortgage 8% Gold Bonds dated August 1, 1920 and due August 1, 1930. These bonds, which will hereinafter be referred to as the "General Mortgage 8's," were, under the provisions of the Mortgage Indenture, convertible under certain conditions into Series [fol. 112] B 7's, and in 1922 the holders of $4,671,100.00 face value thereof actually made such conversion (Cf. paragraph 12). Exhibit "B" attached hereto is a copy of that portion of the Mortgage Indenture which contains the provisions above referred to.

(5) On February 1, 1921, Petitioner executed a third trust indenture, a copy of which is attached hereto and marked Exhibit "C." This indenture will hereinafter be referred to as the "General Lien Indenture."

(6) During the year 1921 Petitioner, pursuant to the provisions of the General Lien Indenture, issued and sold $2,500,000.00 face value of its General Lien 8% Gold Bonds dated February 1, 1921, and due February 1, 1936. These bonds, which will hereinafter be referred to as the "General Lien 8's," were sold at a discount of $150,000.00 and the expense of issuance was $22,283.54. The General Lien 8's, were convertible under certain circumstances into Series B 7's, and on August 1, 1924, the holders of $2,354,500.00 face value thereof actually made such conversion (Cf. paragraph 8).

(7) Prior to December 31, 1923, Petitioner had purchased and retired $11,000.00 face value of the General Lien 8's and the unamortized discount and expense of issuance applicable thereto was charged off as a loss in the year of retirement.

(8) On August 1, 1924, pursuant to a resolution adopted by Petitioner's Board of Directors on May 8, 1924, the [fol. 113] holders of $2,354,500.00 face value of the General Lien 8's exchanged them for a like amount of Series B 7's and received, in addition to the Series B bonds, a

cash premium of $117,725.00. Such exchange was made in accordance with the provisions of the option granted by the General Lien Indenture. A copy of the resolution above referred to is attached hereto as Exhibit "D." The unamortized discount and expense applicable to such converted bonds was, on August 1, 1924, $126,176.97 and the expense of conversion was $1,461.05. The sum of the three items named: to wit, premium paid, unamortized discount and expense and expense of conversion, was $245,363.02, of which the Respondent has allowed as a deduction for the year 1924 only $2,027.96 and for the year 1926 only $8,735.78.

Petitioner contends that the full amount of $245,363.02 is allowable as a deduction for the year 1924, whereas the Respondent contends that such amount should be amortized over the life of the Series B 7's which were exchanged for the General Lien 8's.

Petitioner concedes that if the $245,363.02 be allowed in full as a deduction for the year 1924 then its net income for the year 1926 as shown in the deficiency letter may be increased by the sum of $8,735.78.

(9) As of August 1, 1924, Petitioner purchased for cash and retired all of the General Lien 8's which remained outstanding after the conversion referred to in paragraph 8. These outstanding bonds, which were of a face value of $134,500.00, were purchased by Petitioner at a premium of [fol. 114] $6,725.00; the unamortized discount and expense applicable to such bonds on August 1, 1924, was $7,207.82 and the expense of retirement was $83.46. The sum of the three items named: to wit, premium paid on retirement, unamortized discount and expense, and expense of retirement, is $14,016.28 of which the Respondent has allowed as a deduction for 1924 only $5,464.08. The Respondent now concedes that the balance of $8,552.20 is also an allowable deduction for the year 1924.

(10) During the year 1921 Petitioner issued its second series of bonds under the Refunding Mortgage. These bonds, the Series B 7's, were dated August 1, 1920, and were due August 1, 1950.

(11) The said Series B 7's were issued to a face value of $8,500,000.00 and were disposed of as follows:

Par value	Disposal
$5,000,000.00	Delivered to the trustees under the General Mortgage Indenture and held by them as additional security for the General Mortgage 8's.
$2,500,000.00	Delivered to the trustees under the General Lien Indenture and held by them as additional security for the General Lien 8's.
$1,000,000.00	Sold to the public in 1921 for cash at a discount of $100,000.00.
$8,500,000.00	Total issued.

[fol. 115] The expense of issuing the entire Series B was $49,548.14.

(12) The $5,000,000.00 face value of Series B 7's delivered to the General Mortgage trustees were disposed of by them as follows: $4,671,100.00 face value were exchanged in 1922 for a like amount of General Mortgage 8's outstanding in the hands of the public and the remaining $328,900.00 were returned to Petitioner by reason of the cash redemption after the call date of a like amount of General Mortgage 8's. None of the Series B 7's so returned to Petitioner were thereafter re-issued.

(13) The $2,500,000.00 face value of Series B 7's delivered to the General Lien trustees were disposed of by them as follows: $2,354,500.00 were exchanged on August 1, 1924, for a like amount of General Lien 8's outstanding in the hands of the public and of the remainder, to wit, $145,500.00 face value, $11,000.00 face value were returned to Petitioner by reason of the latter's retirement and delivery to the trustees for cancellation of a like amount of General Lien 8's which Petitioner had purchased from the public for cash, and $134,500.00 were returned to Petitioner by reason of the cash redemption after the call date of a like amount of General Lien 8's. None of the Series B 7's so returned to Petitioner were thereafter reissued. In addition to the $474,400.00 face value of Series B 7's which were reacquired by Petitioner as indicated above, $603,000.00 face value of the Series B 7's were reacquired by [fol. 116] Petitioner prior to June, 1925, and as to such bonds there is no dispute.

(14) In 1925 Petitioner began and consummated a program of partial refinancing which resulted in the retirement of its outstanding Series B 7's and the issuance of a fourth series of bonds under the "Refunding Mortgage." These new bonds, the Series D 5½'s, were dated February 1, 1925, were due February 1, 1955, and bore interest at the rate of 5½% per annum. The following is a tabular analysis of the retirement of the Series B 7's:

Date	Par value of Bonds retired	Premiums Paid in cash	Unamortized Discount and expense	Expense of Retirement
June, 1925	$419,700.00	$43,415.22	$7,399.61	.....
July, 1925	257,400.00	10,863.50	4,523.15	.....
Aug. 1, 1925	6,745,500.00	674,550.00	117,989.72	.....
Totals	$7,422,600.00	$728,828.72	$129,912.48	$9,447.92

The following is a tabular analysis of the issuance of the Series D 5½'s:

Date	Purchaser	Par value	Discount	Expense of issuance
March, 1925	E. H. Rollins & Sons	$1,500,000	$112,500	
June 10, 1925	E. H. Rollins & Sons	6,300,000	315,000	
July 15, 1925	Western Power Corp.	700,000	35,000	$47,094.15
Subsequent to Aug. 1, 1925	E. H. Rollins & Sons	1,000,000	50,000	

All of the Series B 7's were redeemed for cash. The amounts necessary for the June, 1925, and July, 1925, redemptions and for the payment of the expense item of $9,447.92 were taken from the general funds in Petitioner's [fol. 117] treasury. The amount of cash necessary for the August 1, 1925, redemption was $7,420,500.00. This amount was derived from the following sources:

By the previous issuance and sale of $7,000,000.00 face value of Series D 5½'s at a discount of 5%	$6,650,000.00
Petitioner's general funds (Including $141,808.32 representing interest accrued on the $7,000,000.00 of bonds from February 1, 1925, to date of issuance)	770,050.00
	$7,420,050.00

The amounts of $6,650,000.00 and $141,808.32 indicated above as derived from the sale of the Series D 5½'s were not received by the Petitioner, but were paid by the pur-

chasers to the Bank of America and held in escrow until August 1, 1925, and were then paid directly to the trustees under the "Refunding Mortgage."

During the year 1925 the Railroad Commission of California, pursuant to application filed by Petitioner, issued its opinions and orders dated February 5, 1925, May 27, 1925, and October 21, 1925 and numbered respectively 14541, 14979, and 15544, copies of which opinions and orders are attached hereto and marked Exhibit "E", Exhibit "F", and Exhibit "G" respectively. Attached hereto and marked Exhibits "H", "I" and "J" are certified copies of extracts from the Minutes of Special meetings of the Board of Directors of the Petitioner held on February 5, [fol. 118] 1925, May 15, 1925, and September 25, 1925 in reference to the issuance of Petitioner's Series D 5½'s and the retirement of Petitioner's Series B 7's.

(15) Petitioner contends that the sum of the items "Premiums Paid"—$728,828.72, "Unamortized Discount and Expense"—$129,912.48 and "Expense of Retirement"—$9,447.92 shown above in connection with the retirement of the Series B 7's, to wit, $868,189.12, constitutes an allowable deduction for the year 1925. The Respondent contends (a) that said sum of $868,189.12 (including also the unamortized portion of the amounts referred to in paragraph (8) hereof) should be treated as part of the capital cost of refinancing and refunding Petitioner's bonded indebtedness, and should be treated in its entirety as applicable to the Series D 5½'s maturing February 1, 1955, and amortized over the remaining life of the Series D 5½'s; (b) $7,000,000.00 of said sum should be treated as applicable

---

$7,422,600.00

to the Series D 5½'s to be amortized over their remaining life (c) that the sum of $674,550.00, $117,989.72, and $6,745,500.00 of the expense of retirement and the unamor-

---

$7,422,600.00

tized portion of the amounts referred to in paragraph (8) hereof should be treated as applicable to the Series D 5½'s and amortized over their remaining life; or (d) that at least $6,650,000.00 of the amount referred to in (c) should be

---

$7,420,650.00

treated as applicable to the Series D 5½'s and amortized over their remaining life.

[fol. 119] (16) In determining the deficiencies for the years 1924, 1925 and 1926 the Commissioner allowed deductions in respect of Petitioner's General Lien 8's, Series B 7's, and Series D 5½'s as indicated below:

Description	1924	1925	1926
General Lien 8's:			
Amortization of discount and expense on outstanding bonds	*$6,765.90	.....	.....
Loss on retirement	5,464.08 (See par. 9)	.....	.....
"B 7's" Account General Lien 8's:			
Amortization of premiums, discount and expense on General Lien 8's converted into Series B 7's on Aug. 1, 1924	2,027.96 (See par. 8)	.....	.....
Series B 7's:			
Amortization of discount and expense on outstanding bonds	*5,227.32	*$3,039.57	.....
Loss on bond retirements (Prior to June, 1925)	.....	*4,046.56	.....
"D 5½'s" Account Series B:			
Amortization of amounts referred to in par. (8) hereof	.....	.....	$8,735.78 (See par. 8)
Series D 5½'s:			
Amortization of discount and expense of issuance	.....	*9,047.44	*18,782.28
Loss on bond retirements prior to December 31, 1925	.....	*3,714.34	.....

* There is no dispute between the parties with reference to these items.

[fol. 120] (17) In addition to the adjustments to petitioner's tax liability which may result from the foregoing facts, petitioner is entitled to the following deductions from the amounts of net income indicated in the notice of deficiency:

1924

Item	Additional allowance
Contribution to Industrial Association of San Francisco	$ 720.00
Contribution to Californians, Inc.	500.00
Total	$1,220.00

1925

Additional interest deduction, being the excess of the interest payable from the effective date of the Series D 5½'s to August 1, 1925, over the amount of interest received from the funds realized from the sale of said bonds	$26,558.76
Total	$26,558.76

1926

Loss on purchase and retirement of petitioner's bonds:

[fol. 121] $32,500 face value Series A6's	$4,187.31
$49,000 face value Series C6's	4,542.32
$48,000 " " Series D5½'s	3,260.05*
Loss on purchase of $28,000 Calif. Elec. Gen. bonds as per rental agreement	202.50
Gain on purchase of:	
$7,450 Consolidated Electric General Mortgage Bonds (Gain)	234.00
$1,000 Central Oakland Light (Gain)	30.00
Total	$11,928.18

(18) In the event that it be determined that Petitioner sustained an operating loss for the calendar year 1925 it is agreed that for the purpose of computing the net loss under Sec. 206 of the Revenue Act of 1926 to be deducted from Petitioner's net income for the calender year 1926, such operating loss should be adjusted on account of the following items:

[fol. 122] Dividends of domestic corporations	$ 50.00
Non-taxable interest on obligations of the United States	2,087.21
Total adjustment	$2,137.21

* (If it should be determined that any portion of the unamortized discount and expense of issuance, premiums paid, and expense of retirement of the General Lien 8's and/or Series B 7's should be carried over into the Series D5½'s, then this amount will be increased accordingly. Said $48,000 of Series "D" 5½'s were purchased and retired April 27, 1926.)

(19) Subject to petitioner's objection on the grounds of relevancy and materiality, the parties hereto stipulate the following facts:

(a) That the amounts of unamortized discount and expense, premiums paid, and expense of retirement applicable to the General Lien 8's referred to in paragraph 8 hereof were not charged to profit and loss on petitioner's books, but were transferred to "Discount and Expense Series B Account General Lien" to be amortized over the remaining life of the Series B 7's.

(b) That the amounts of unamortized discount and expense (including the unamortized portion of the amounts referred to in sub-paragraph [a]), premiums paid, and expense of retirement applicable to the Series B 7's referred to in paragraph (14) hereof were not charged to profit and loss on petitioner's books, but were transferred to "Discount and Expense Series D 5½'s Account Series B 7's" to be amortized over the remaining life of the Series D 5½'s.

So far as pertinent and material, the various exhibits mentioned in the foregoing Stipulation of Facts No. 2, viz., Exhibits A, A-1, A-2, A-3, A-4, B, C, D, E, F, G, H, I and J, are as follows:

[fol. 123] EXHIBIT A, ANNEXED TO FOREGOING STIPULATION OF FACTS

Refunding Mortgage

Dated March 1, 1919

(Condensed)

This exhibit consists of a printed trust indenture whereby Great Western Power Company of California (therein called the Company) conveyed and mortgaged all its property then owned or thereafter acquired to Bankers Trust Company, a corporation of the State of New York, as Trustee, for the benefit and security of the holders of the bonds to be issued from time to time thereunder and designated as "First and Refunding Mortgage Sinking Fund Gold Bonds". The recitals of the indenture are in part as follows:

"Whereas, the Company has deemed it necessary to borrow money for its corporate purposes and to make provision for the borrowing of additional money from time to time to enable it to acquire or construct additional plants and property and improvements, extensions and additions to or about its plants or property and to refund, pay, purchase or otherwise acquire mortgage or other liens which may exist thereon and to acquire bonds, notes and other obligations and shares of stock of other corporations; and

"Whereas, the Company has deemed it necessary to provide for the issuing of bonds for the money so to be borrowed and to mortgage all of its property now owned or [fol. 124] hereafter acquired to secure the payment of said bonds and to that end has duly authorized and directed the issue from time to time of bonds unlimited in aggregate principal amount (except as hereinafter provided) to be designated as its 'First and Refunding Mortgage Sinking Fund Gold Bonds' (except as hereinafter in Section 1 of Article XVI provided), such bonds to be coupon bonds or registered bonds without coupons, to be issued under this indenture in any number of series and (with respect to each series) to be of such denominations, issued and dated at such time or times, bear such rate of interest, mature at such time or times (not later than March 1, 1979), and be subject to redemption and/or conversion on such terms, as the board of directors of the Company may determine as to each series thereof prior to, or concurrently with, the application of the Company to the Trustee for certification and delivery of the bonds proposed to be issued and sold and the terms of which have been so fixed; all of such bonds to be signed in the Company's corporate name by its president or a vice-president, to be impressed with its corporate seal, attested by its secretary or an assistant secretary, and to be certified by the Trustee; which coupon bonds, coupons, registered bonds without coupons, and Trustee's certificates are to be substantially in the forms following respectively; appropriate insertions, omissions and variations to be made in respect of the form and terms of the [fol. 125] bonds and coupons of each series in accordance with resolutions of the board of directors of the Company, as hereinafter provided, to express the terms and conditions on which such bonds are issued as required or permitted by this indenture: (Setting out prescribed forms for coupon bonds and registered bonds.)"

Provision was made for annual payments to be made to the Trustee, equal to 1½% of all bonds outstanding under the indenture, such payments together with interest to constitute a sinking fund to be applied by the Trustee partly for the purchase or redemption of bonds and partly for other specified purposes as directed by the Company. The indenture also contains various other covenants, conditions and provisions defining the duties, rights and remedies of the Company, the Trustee and the bondholders, including the following:

"[Art I, Sec. 1] * * *

"Bonds of any series may contain such provisions, if any, in respect of payment of principal and/or interest without deduction for taxes or other charges and/or in respect of conversion thereof into shares of stock and/or other bonds, notes or other obligations of the Company, as may be lawful and determined by the board of directors of the Company in accordance with the provisions of this indenture. As to each series of bonds issued hereunder the board of [fol. 126] directors of the Company may fix, among other things, the date and the maturity (not later than March 1, 1979) of such bonds, the denomination or denominations in which the same shall be issued and the interest rate and redemption price and dates and may determine whether such series shall consist of coupon bonds, registered bonds without coupons, or both, and whether such bonds shall be convertible and, if so, upon what terms and conditions, all in accordance with the provisions of this indenture."

"[Art. I, Sec. 2] The bonds issued hereunder may be issued in series and the bonds and coupons of each series shall be designated by a distinguishing letter of the English alphabet and such further designation as the board of directors may fix and determine. All bonds of any one series at any time simultaneously outstanding shall be identical in respect of date, maturity, interest rate, redemption price and dates and other terms except that bonds of the same series may be of different denominations and may include both coupon bonds and registered bonds without coupons."

"[Art. I, Sec. 5] All (but not less than all) of the bonds of any series at any time issued under Section 2 or Section 3 of Article II hereof and then outstanding under this indenture may, at the option of the Company evidenced by

[fol. 127] a copy of a resolution certified to have been adopted by the board of directors of the Company filed with the Trustee, be made exchangeable (at the option of the holders), upon such terms and conditions and during such period of time (not less than that hereinafter in this Section 5 provided) as shall be specified in such resolution, for other bonds of some other series issuable hereunder of an equal aggregate principal amount. Such resolution shall specify also the series designation of the bonds for which such outstanding bonds are so exchangeable, their denominations (which shall be the same as those of such outstanding bonds), date, maturity (not earlier than ten years after the issuance thereof), interest rate, redemption price and dates and other terms (in compliance with the provisions of this indenture). Notice of such privilege of exchange and of the terms and conditions thereof shall be given by or on behalf of the Company by publication at least once a week for four successive weeks in one newspaper of general circulation published in the Borough of Manhattan, City of New York, and such privilege of exchange shall continue at least three months after the date of the first publication of such notice. In such case, upon the request of the holders of any of such outstanding bonds and upon the surrender of such bonds (with all unmatured coupons thereto belonging) to the Trustee for such exchange, the Company shall execute and deliver to the Trustee and the Trustee shall, as speci-
[fol. 128] fied in such resolution, certify and deliver bonds for the purpose of such exchange. In case of any such exchange the Trustee shall forthwith cancel the surrendered bond or bonds and the accompanying coupons, and deliver the same to the Company on its written request."

"[Art. II, Sec. 1] This indenture constitutes a continuing lien to secure the full and final payment of the principal and interest of all bonds which may, from time to time, be made, certified, delivered and issued hereunder as well as for the observance and performance of all the covenants, agreements and conditions herein contained. The principal amount of bonds which may be so made, certified, delivered and issued hereunder is not limited except as hereinafter specifically set forth. All bonds issued under and in pursuance of this indenture and at any time outstanding shall in all respects (subject to the provisions of this indenture

relating to matured coupons purchased, extended or transferred or pledged separate or apart from the bond to which they relate) be equally and ratably secured hereby without preference, priority or distinction on account of the actual time or times of the issue of the said bonds, or any of them, so that all bonds at any time issued and outstanding hereunder shall have the same right, lien and preference under and by virtue of this indenture, and shall all be equally [fol. 129] secured hereby with like effect as if they had all been made, certified, delivered and issued simultaneously on the date hereof, whether the same, or any of them, shall be actually sold or disposed of at such date, or whether they, or any of them, shall be made, certified, delivered and issued, and sold or disposed of at some future date or dates, or whether they or any of them shall have been authorized to be issued under the provisions of Section 2 of this Article II relating to the initial issue of bonds hereunder or may be authorized to be issued hereafter pursuant to the provisions of Section 3 or Section 4 or Section 5 of this Article II."

"[Art. II, Sec. 2] The initial issue of bonds hereunder shall be designated as Series A, and the aggregate principal amount thereof shall be $6,000,000. [illegible]v shall be dated concurrently herewith, shall bear inte[illegible]e rate of six per cent. per annum from such date, shall mature on the first day of March, 1949, and shall be redeemable on the first day of any month upon sixty days' published notice, upon payment of the principal, accrued interest and, if redeemed before March 1, 1939, a premium of three per cent. of the principal, if redeemed on or after March 1, 1939, and before March 1, 1948, a premium of two per cent., and if redeemed on or after March 1, 1948, and before March 1, 1949, without a premium. * * *"

[fol. 130] "[Art. II, Sec. 3] From time to time hereafter the Company may execute and deliver to the Trustee, and the Trustee shall certify and deliver to the Company, additional bonds secured hereby * * *. [Here follow various conditions and limitations with respect to the acquisition of additional properties, the sufficiency of the Company's earnings, and the adoption and furnishing of certain resolutions, certificates and reports.]"

"[Art. II, Sec. 9] From time to time hereafter the Company may execute and deliver to the Trustee, and the Trustee shall upon the order of the Company evidenced by a copy of a resolution certified to have been adopted by the board of directors of the Company filed with the Trustee, specifying the principal amount of bonds called for, the series designation thereof, their denominations, date, maturity, interest rate, redemption price and dates and other terms (in compliance with the provisions of this indenture), certify and deliver additional bonds secured hereby upon deposit with the Trustee by the Company of cash equal to the principal amount of the bonds so ordered to be certified and delivered; provided, however, that the aggregate amount of such cash on deposit with the Trustee under the provisions of this Section 9 shall not at any one time exceed the sum of six million dollars * * *."

"[Art. III, Sec. 2] The Company hereby covenants and agrees * * *:

[fol. 131] "That it will pay the principal and interest of all the bonds duly issued hereunder, according to the terms thereof * * *."

"[Art. V] Redemption of Bonds. The Company, at its option, may from time to time in accordance with the terms of the bonds issued hereunder redeem all or any of such bonds, at the redemption price specified therein respectively (including accrued interest to the redemption day), provided that in case of redemption of a part only of any series of bonds the particular bonds to be redeemed shall be selected by the Trustee by lot; in the event that the Company elects at any time to redeem less than all the bonds then outstanding hereunder, it may designate the series from which the redemption shall be made. Notice of intention to redeem (including in case a part only of any series of bonds are to be redeemed, the numbers of such bonds) shall be given by or on behalf of the Company, by publication immediately preceding the date fixed for redemption, in accordance with the terms of the bonds called for redemption, in one newspaper of general circulation published in the Borough of Manhattan, City of New York, and one in each other city where any bonds called for redemption are payable. Before such redemption day specified in such notice, the Company shall deposit with the Trus-

tee an amount sufficient to redeem the bonds so designated for redemption on such date to be held for account of the [fol. 132] holders thereof and to be paid to them respectively upon presentation and surrender of said bonds with all unmatured coupons thereto belonging. After such redemption day and such deposit such bonds shall cease to bear interest, and shall cease to be entitled to the lien of this indenture, and the coupons for interest maturing subsequent to that day shall be void.

* * * * * * *

"All bonds secured hereby so redeemed shall forthwith be cancelled, and the Trustee shall note hereon or on one of the originals hereof the fact of such cancellation, and thereupon deliver the bonds so cancelled to the Company."

"[Art. XVI, Sec. 6] All premiums paid for the redemption of bonds, pursuant to the provisions hereof, shall be computed upon the principal amount of such bonds exclusive of interest. The principal amount of new bonds to be issued upon an exchange of bonds hereunder or to be issued against bonds deposited with the Trustee shall be determined by the principal amount exclusive of interest of the bonds surrendered for exchange or deposited hereunder."

[fol. 133] EXHIBIT A-1, ANNEXED TO FOREGOING STIPULATION OF FACTS

Resolutions of December 7, 1920

(In Full Except Certification)

Whereas, under the First and Refunding Mortgage of this corporation to Bankers Trust Company, as Trustee, dated March 1, 1919, there have been issued and are now outstanding $6,000,000 in aggregate principal amount of bonds, being the initial issue of bonds designated as Series A provided for by Section 2 of Article II of said mortgage: and

Whereas this corporation has, for a valuable consideration, obligated itself to make provision for the issuance of a second series of bonds to be secured, when issued, by

said First and Refunding Mortgage, said second series of bonds to be designated as Series B, to be issued in the denominations and have the date, maturity, interest rate, redemption prices and dates and other terms (in compliance with the provisions of said mortgage) hereinafter provided, and has likewise obligated itself to make provision for the issuance of $5,000,000 in aggregate principal amount of said bonds of Series B:

Now therefore, be it resolved, that the second series of bonds to be secured, when issued, by said mortgage shall be designated as Series B; shall be dated August 1, 1920, shall bear interest at the rate of seven per cent per annum from said date, pavable semi-annually on February 1 and August 1 of each year; shall mature on the 1st day of August, [fol. 134] 1950; shall be redeemable, at the option of this corporation, on any interest date upon sixty days' published notice, upon payment of principal and accrued interest and if redeemed on or before August 1, 1930, a premium of ten per cent of the principal; and if redeemed after August 1, 1930, a premium of one-half of one per cent of the principal for each full year of the unexpired term of said bonds; shall be coupon bonds of $1,000 each, numbered from M-1 upwards, of $500 each, numbered from D-1 upwards and of $100 each, numbered from C-1 upwards;

Further resolved, that this corporation shall covenant to pay all taxes which, by any present or future law of the United States, or of any state, county, municipality or other governmental subdivision therein, it may be required to pay upon or authorized or permitted to retain from the principal of or interest upon said Series B bonds, except inheritance and/or succession taxes and except Federal income taxes in excess of two per cent per annum;

Further Resolved, that the principal of said bonds of said Series B shall be payable at the office of this corporation in the City of San Francisco, or at its office or agency in the Borough of Manhattan, City of New York, at the option of the bearer or holder, and that the interest thereon shall be payable at either of said places, or at the office or agency of this corporation in the City of Boston, or in the City of Chicago, at the option of the bearer or holder;

[fol. 135] Further Resolved, that the form of said Series B bonds, of the coupons attached thereto and of the trus-

tee's certificate and of the registration endorsement endorsed thereon shall be substantially in the forms following, respectively, appropriate insertions and variations to be made in respect of the number and denomination of said bonds, and in respect of the number, par value and maturity of said coupons:

(Form of Bonds)

UNITED STATES OF AMERICA,
State of California:

Great Western Power Company of California

First and Refunding Mortgage Sinking Fund Gold Bond
Seven Per Cent. Due August 1, 1950

Series B

No. —. $ —.

Great Western Power Company of California, hereinafter called the 'Company', for value received, promises to pay to the bearer, or, if this bond be registered, to the registered holder hereof, on the first day of August, 1950, at the office of the Company, in the City of San Francisco, or at its office or agency in the Borough of Manhattan, City of New York, at the option of the bearer or registered holder — Dollars in gold coin of the United States of America, of [fol. 136] the standard weight and fineness obtaining on August 1, 1920, and to pay interest thereon from the date hereof at the rate of seven percentum per annum, in like gold coin at the office of the company in the City of San Francisco, or at its office or agency in the Borough of Manhattan, City of New York, or in the City of Boston or in the City of Chicago, on the first days of February and August in each year, according to the tenor of the respective coupons hereto attached and upon presentation and surrender thereof, until such principal shall be paid.

The Company promises to pay all taxes which, by any present or future law of the United States or of any state, county, municipality or other governmental subdivision therein, it may be required to pay upon or authorized or permitted to retain from, the principal of or interest on this bond, except inheritance and/or succession taxes and ex-

cept Federal Income taxes in excess of two per centum per annum.

This bond is one of a series of bonds which, together with all other series which have been or may be issued thereunder (and which may include both coupon bonds and registered bonds without coupons), are known as the "First and Refunding Mortgage Sinking Fund Gold Bonds" of the Company, all issued and to be issued under and equally secured by a Mortgage and Deed of Trust, hereinafter called the "Mortgage", dated March 1, 1919, duly executed [fol. 137] by the Company to Bankers Trust Company, as Trustee, to which this bond is subject and to which reference is made for a description of the property mortgaged and pledged, the nature and extent of the security, the rights of the holders of the bonds and the terms and conditions upon which the bonds are issued and secured.

This bond is subject to redemption, as provided in the Mortgage on any interest date upon sixty days' published notice, upon payment of the principal, accrued interest and, if redeemed on or before the 1st day of August, 1930, a premium of ten per cent of the principal; and if redeemed after the 1st day of August, 1930, a premium of one-half of one per centum for each full year of its then unexpired term. This bond is entitled to the benefits of the Sinking Fund provided for in the Mortgage. The principal hereof may also become due on the conditions and in the manner and at the time and with the effect set forth in the Mortgage, in case of certain defaults specified in the Mortgage.

Unless registered as herein provided, this bond shall pass by delivery. This bond may be registered as to principal in the owner's name upon the books of the company at its said office or agency in the Borough of Manhattan, City of New York, such registration being noted hereon, after which no valid transfer hereof can be made, except on said books, the new registration being similarly noted hereon, [fol. 138] until after registered transfer to bearer, but after such registered transfer to bearer, this bond shall be again transferable by delivery. Such registration, however, shall not affect the negotiability of the coupons which shall always be payable to bearer and transferable by delivery.

No recourse shall be had for the payment of the principal of or interest on this bond against any stockholder,

officer or director of the Company, either directly or through the Company, under any statute or by the enforcement of any assessment or otherwise, all such liability of stockholders, directors and officers being released by the holder hereof by the acceptance of this bond and being likewise waived and released by the terms of the Mortgage.

This bond shall not become obligatory until Bankers Trust Company, the Trustee under the Mortgage, or a successor trustee thereunder, shall have signed the form of trustee's certificate endorsed hereon.

In Witness Whereof, Great Western Power Company of California has caused this bond to be signed in its name by its President or a Vice-President, and its corporate seal to be hereunto affixed and attested by its Secretary or an Assistant Secretary, and interest coupons bearing the engraved signature of its Treasurer to be attached hereto [fol. 139] and this bond to be dated this first day of August, 1920.

Great Western Power Company of California, by —— ——, President.

Attest: —— ——, Secretary.

(Form of Coupons)

No. —. $ —.

On the — day of ——, 19—, Great Western Power Company of California will pay to bearer at its office in the City of San Francisco or at its office or agency in the Borough of Manhattan, City of New York, or in the City of Boston, or in the City of Chicago, — Dollars in gold coin of the United States, without deduction for taxes, except as specified in its First and Refunding Mortgage Sinking Gold Bond No. ——, Series B, being six months' interest then due on said bond.

This coupon will not be payable if said bond shall have been called for previous redemption.

—— ——, Treasurer.

[fol. 140] (Form of Trustee's Certificates)

This is to certify that this bond is one of the bonds described in the within mentioned mortgage.

Bankers Trust Company, Trustee, by —— ——, Assistant Secretary.

(Form of Registration Indorsement)

Notice: No writing on this form except by an officer of the trustee

Date of Registry	In Whose Name Registered	Registrar
.....	.....	.....
.....	.....	.....
.....	.....	.....

Further resolved, that upon each of said Series B Bonds of the denomination of $100 and $500, there shall be endorsed substantially the following legend:

"The holder of this bond may at his option on surrender and cancellation of this bond and others of the same series aggregating One Thousand Dollars and on payment of charges as provided in the above mentioned mortgage, receive in exchange a coupon bond of this series of a number [fol. 141] not contemporaneously outstanding for One Thousand Dollars."

Further resolved, that a fac-simile signature of the present treasurer of this corporation be and hereby is adopted for a coupon signature and such fac-simile signature shall be engraved upon each of such coupons;

Further resolved, that $5,000,000 in aggregate face amount of said bonds of Series B, being 4550 bonds for $1,000 each numbered from M-1 to M-4550, inclusive, 750 bonds for $500 each numbered from D-1 to D-750, inclusive, and 750 bonds for $100 each numbered from C-1 to C-750, inclusive, shall be forthwith executed by the president or vice-president of this corporation and impressed with its corporate seal, attested by its secretary or assistant secretary, and delivered to Bankers Trust Company, trustee under said mortgage, to be held by it until said Trustee shall be required to certify and deliver the same from time to time to this corporation or upon its order as provided in Article II of said mortgage.

Further resolved, that pending the preparation of permanent bonds, there shall be executed by the president or vice-president of this corporation and impressed with its corporate seal, attested by its secretary or assistant secretary, and delivered to said Bankers Trust Company, in

lieu of the bonds in the last preceding resolution referred to, temporary bonds substantially of the tenor of the bonds hereinbefore described and set forth, except that no coupons [fol. 142] shall be attached thereto, and that 200 of such temporary bonds shall be for the principal amount of $1,000 each, numbered consecutively from A-1 to A-200, inclusive, and 48 thereof shall be for the principal amount of $100,000 each, numbered consecutively from B-1 to B-48, inclusive.

EXHIBIT A-2, ANNEXED TO FOREGOING STIPULATION OF FACTS

Resolutions of April 8, 1921

(In Full Except Certification)

Whereas, this corporation has heretofore made provision for the issuance of $5,000,000 in aggregate principal amount of its First and Refunding Mortgage Sinking Fund Gold Bonds of Series B; and

Whereas, this corporation has, for a valuable consideration, obligated itself to make provision for the issuance of an additional $2,500,000 in aggregate principal amount of said bonds of Series B;

Now therefore, be it resolved, that an additional $2,500,000 in aggregate principal amount of said bonds of Series B, being 2225 bonds for $1,000 each, numbered from M-4551 to M-6775, inclusive for 500 bonds for $500 each, [fol. 143] numbered from D-751 to D-1250, inclusive, and 250 bonds for $100 each, numbered from C-751 to C-1000, inclusive, shall be forthwith executed by the president or any vice-president of this corporation and impressed with its corporate seal, attested by its secretary or assistant secretary and delivered to Bankers Trust Company, Trustee, under the First and Refunding Mortgage of this corporation, dated March 1, 1919, to be held by said Trustee until it shall be required to certify and deliver the same from time to time to this corporation or upon its order as provided in Article II of said mortgage.

EXHIBIT A-3, ANNEXED TO FOREGOING STIPULATION OF FACTS

Resolutions of June 21, 1921

(In Full Except Certification)

Whereas, this corporation, Great Western Power Company of California, has heretofore made provision for the issuance of $7,500,000 in aggregate principal amount of its First and Refunding Mortgage Sinking Fund Gold Bonds of Series B; and

Whereas, this Board of Directors deems it necessary to make provision for the issuance of an additional $2,500,000 in aggregate principal amount of said bonds of Series B; [fol. 144] Now therefore, be it resolved, that an additional $2,500,000 in aggregate principal amount of said bonds of Series B, being 2225 bonds for $1,000 each, numbered from M-6776 to M-9000, inclusive, 500 bonds for $500 each, numbered from D-1251 to D-1750, inclusive, and 250 bonds for $100 each, numbered from C-1001 to C-1250, inclusive, shall be forthwith executed by the president or any vice-president of this corporation and impressed with its corporate seal, attested by its secretary or any assistant secretary and delivered to Bankers Trust Company, Trustee under the First and Refunding Mortgage of this corporation, dated March 1, 1919, to be held by said Trustee until it shall be required to certify and deliver the same from time to time to this corporation or upon its order as provided in Article II of said mortgage.

EXHIBIT A-4, ANNEXED TO FOREGOING STIPULATION OF FACTS

Resolutions of February 5, 1925

(In Full Except Certification)

Whereas, under the First and Refunding Mortgage made by this corporation to Bankers Trust Company as Trustee, dated March 1, 1919, there have been authorized $6,000,000 in aggregate principal amount of bonds dated March 1, 1919, designated as Series "A", and $10,- [fol. 145] 000,000 in aggregate principal amount of bonds dated August 1, 1920, designated as Series "B", and $9,-

000,000 in aggregate principal amount of bonds dated February 1, 1922 designated as Series "C"; and

Whereas, this corporation has for a valuable consideration obligated itself to make provision for the issuance of a fourth series of bonds to be secured when issued by said First and Refunding Mortgage, said fourth series of bonds to be designated as Series "D", to be issued in the denominations and have the date, maturity, interest rate, redemption prices and dates and other terms (in compliance with the provisions of said mortgage) hereinafter provided and has likewise obligated itself to make provision for the issuance of $1,500,000 in aggregate principal of said bonds of Series "D";

Now, therefore, be it resolved, that the fourth series of bonds to be secured when issued by said First and Refunding Mortgage shall be designated as Series "D"; shall be dated February 1, 1925; shall bear interest at the rate of five and one-half per cent per annum from said date, payable semi-annually on February 1 and August 1 of each year; shall mature on the first day of February, 1955; shall be redeemable at the option of this corporation on the first day of any month upon sixty days' published notice, upon payment of the principal, accrued interest and, if redeemed before the 1st day of February, 1935, a premium of two and [fol. 146] one-half per cent of the principal; and if redeemed on or after the 1st day of February, 1935, a premium of one-eighth of one per cent for each year or fraction of a year of its then unexpired term.

Further resolved, that said bonds shall be coupon bonds of $1,000 each numbered from M-1 upwards, $500 each numbered from D-1 upwards and $100 each numbered from C-1 upwards;

Further resolved, that this corporation shall covenant to pay all taxes which, by any present or future law of the United States, or of any state, county, municipality or other governmental subdivision therein, it may be required to pay upon or authorized or permitted to retain from the principal of or interest upon said Series D bonds, except inheritance and/or succession taxes and except Federal income taxes in excess of two per centum per annum;

Further resolved, that this corporation shall covenant to reimburse (a) to any holder of any of said bonds who shall be a resident of the Commonwealth of Pennsylvania, when paid by him, any personal property taxes assessed under the laws of said Commonwealth upon said bonds or upon such holder as a resident of said Commonwealth by reason of his ownership thereof, not in any calendar year in excess of four (4) mills upon each dollar of the principal amount of said bonds, and (b) to any holder of any of said bonds who shall be a resident of the Commonwealth of Massa- [fol. 147] chusetts, when paid by him, any income taxes assessed by said Commonwealth upon such holder by reason of his ownership of said bonds, not in any year in excess of six (6) per centum of the income derived in that year by such holder from the interest thereon; provided that within sixty (60) days after the date of the payment of any such tax, such owner shall file with the Company at its office or agency in the Borough of Manhattan, City and State of New York, the written request of such owner for such reimbursement, accompanied by proof of the facts entitling such owner thereto; and provided that in no event shall the Company be obligated to reimburse any such owner for any interest or penalty assessed upon or paid by him in addition to the amount of such tax as originally assessed;

Further resolved, that the principal of said bonds of said Series D shall be payable at the office of this corporation in the City of San Francisco, or at its office or agency in in the Borough of Manhattan, City of New York, at the option of the bearer or holder, and that the interest thereon shall be payable at either of said places, or at the office of agency of this corporation in the City of Boston, or in the City of Chicago, at the option of the bearer or holder;

Further resolved, that the form of said Series D bonds, of the coupons attached thereto and of the trustee's certificate and of the registration endorsement inscribed thereon shall be substantially in the forms following, respectively, appropriate insertions and variations to be made in respect [fol. 148] of the number and denomination of said bonds, and in respect of the number, par value and maturity of said coupons;

(Form of Bonds)

UNITED STATES OF AMERICA,
State of California:

Great Western Power Company of California

First and Refunding Mortgage Sinking Fund Gold Bond

Five and One-Half Per Cent

Due February 1, 1955

Series D

No. —. $—.

Great Western Power Company of California, hereinafter called the "Company", for value received, promises to pay to the bearer, or, if this bond is registered, to the registered holder hereof, on the first day of February, 1955, at the office of the Company, in the City of San Francisco, or at its office or agency in the Borough of Manhattan, City of New York, at the option of the bearer or registered holder — Dollars in gold coin of the United States of America, of the standard of weight and fineness obtaining on February 1, 1925, and to pay interest thereon from the [fol. 149] date hereof at the rate of five and one-half per centum per annum, in like gold coin at the office of the Company in the City of San Francisco, or at its office or agency in the Borough of Manhattan, City of New York, or in the City of Boston or in the City of Chicago, at the option of the bearer or registered holder, on the first days of February and August in each year, according to the tenor of the respective coupons hereto attached and upon presentation and surrender thereof, until such principal shall be paid.

The Company promises to pay all taxes which, by any present or future law of the United States or of any state, county, municipality or other governmental subdivision therein, it may be required to pay upon or authorized or permitted to retain from, the principal of or interest on this bond, except inheritance and/or succession taxes and except Federal income taxes in excess of two per centum per annum.

The Company will reimburse (a) to any holder of this bond who shall be a resident of the Commonwealth of Pennsylvania when paid by him, any personal property taxes assessed under the laws of said Commonwealth upon this bond or upon such holder as a resident of said Commonwealth by reason of his ownership hereof not in any calendar year in excess of four (4) mills upon each dollar of the principal amount of this bond, and (b) to any holder of this bond who shall be a resident of the Commonwealth of Massachusetts, when paid by him, any income taxes as- [fol. 150] sessed by said Commonwealth upon such holder by reason of his ownership of this bond, not in any year in excess of six (6) per centum of the income derived in that year by such holder from the interest hereon; provided that within sixty (60) days after the date of the payment of any such tax, such owner shall file with the Company at its office or agency in the Borough of Manhattan, City and State of New York, accompanied by proof of the facts entitling such owner thereto; and provided that in no event shall the Company be obligated to, reimburse any such owner for any interest or penalty assessed upon or paid by him in addition to the amount of such tax as originally assessed.

This bond is one of a series of bonds which, together, with all other series which have been or may be issued thereunder (and which may include both coupon bonds and registered bonds without coupons) are known as the "First and Refunding Mortgage Sinking Fund Gold Bonds" of the Company, all issued and to be issued under and equally secured by a Mortgage and Deed of Trust, hereinafter called the "Mortgage", dated March 1, 1919, duly executed by the Company to Bankers Trust Company, as Trustee, to which this bond is subject and to which reference is made for a description of the property mortgaged and pledged, the nature and extent of the security, the rights of the holders of the bonds and the terms and conditions upon which the bonds are issued and secured.

[fol. 151] This bond is subject to redemption, as provided in the Mortgage, on the first day of any month upon sixty (60) days' published notice, upon payment of the principal, accrued interest and, if redeemed before the 1st day of February, 1935, a premium of two and one-half per cent

of the principal; and if redeemed on or after the 1st day of Feb., 1935, a premium of one-eighth of one per cent for each year or fraction of a year of its then unexpired term. This bond is entitled to the benefits of the Sinking Fund provided for in the mortgage. The principal hereof may also become due on the conditions and in the manner and at the time and with the effect set forth in the Mortgage, in case of certain defaults specified in the Mortgage.

Unless registered as herein provided, this bond shall pass by delivery. This bond may be registered as to principal in the owner's name upon the books of the company at its said office or agency in the Borough of Manhattan, City of New York, such registration being noted hereon, after which no valid transfer hereof can be made, except on said books, the new registration being similarly noted hereon, until after registered transfer to bearer, but after such registered transfer to bearer, this bond shall be again transferable by delivery. Such registration, however, shall not affect the negotiability of the coupons which shall always be payable to bearer and transferable by delivery. [fol. 152] No recourse shall be had for the payment of the principal of or interest on this bond against any stockholder, officer or director of the Company, either directly or through the Company under any statute or by the enforcement of any assessment or otherwise, all such liability of stockholders, directors and officers being released by the holder hereof by the acceptance of this bond and being likewise waived and released by the terms of the Mortgage.

This bond shall not become obligatory until Bankers Trust Company, the Trustee under the mortgage, or a successor trustee thereunder, shall have signed the form of trustee's certificate endorsed hereon.

In witness whereof, Great Western Power Company of California has caused this bond to be signed in its name by its President or a Vice-President, and its corporate seal to be hereunto affixed and attested by its Secretary or an Assistant Secretary, and interest coupons bearing the facsimile signature of its Treasurer to be attached hereto and this bond to be dated the first day of February, 1925.

Great Western Power Company of California, by
—— ——, President.

Attest: —— ——, Secretary.

[fol. 153] (Form of Coupons)

No. —. $—.

On the — day of ——, 19—, Great Western Power Company of California will pay to bearer at its office in the City of San Francisco or at its office or agency in the Borough of Manhattan, City of New York, or in the City of Boston, or in the City of Chicago, at holder's option, — Dollars in gold coin of the United States, without deduction for taxes, except as specified in its First and Refunding Mortgage Sinking Fund Gold Bond No. —, Series D, being six months' interest then due on said bond.

This coupon will not be payable if said bond shall have been called for previous redemption.

—— ——, Treasurer.

(Form of Trustee's Certificate)

This is to certify that this bond is one of the bonds described in the within mentioned mortgage.

Bankers Trust Company, Trustee, by —— ——, Assistant Secretary.

[fol. 154] (Form of Registration Endorsement)

Notice: No writing on this form except by an officer of the trustee.

Date of Registry	In Whose Name Registered	Registrar
.....	.....	.....

Further resolved, that upon each of said Series D Bonds of the denomination of $100 and $500, there shall be endorsed substantially the following legend:

"The holder of this bond may at his option on surrender and cancellation of this bond and others of the same series aggregating One Thousand Dollars and on payment of charges as provided in the above-mentioned mortgage, receive in exchange a coupon bond of this series of a number not contemporaneously outstanding for One Thousand Dollars."

Further resolved, that a facsimile signature of the present treasurer of this corporation be and hereby is adopted for a coupon signature and such facsimile signature shall be engraved upon each of such coupons.

Further resolved, that $1,500,000 in aggregate face amount of said bonds of Series D, being 1402 bonds for [fol. 155] $1,000 each, numbered from M-1 to M-1402, inclusive, 180 bonds for $500 each, numbered from D-1 to D-180, inclusive, and 80 bonds for $100 each, numbered from C-1 to C-80, inclusive, shall be forthwith executed by the President or Vice-President of this corporation and impressed with its corporate seal, attested by its Secretary or Assistant Secretary and delivered to Bankers Trust Company, Trustee under said mortgage, to be held by it until said Trustee shall be required to certify and deliver same from time to time to this corporation, or upon its order, as provided in Article II of said mortgage.

EXHIBIT B, ANNEXED TO FOREGOING STIPULATION OF FACTS

Mortgage Indenture

Dated August 1, 1920

(Condensed)

This exhibit consists of copies of the title page and pages 39, 40, 52, 53, 54 and 55 of a printed trust indenture between Great Western Power Company of California and the Equitable Trust Company of New York, Trustee, and Anglo-California Trust Company, Co-Trustee, securing an authorized issue of $5,000,000 General Mortgage Convertible Eight Per Cent Gold Bonds dated August 1, 1920, known as "General Mortgage 8's". Pertinent provisions con- [fol. 156] tained therein with respect to the deposit of Series B 7% bonds of the Company, and with respect to the redemption of the General Mortgage 8's, and their conversion into Series B 7's, are as follows:

And the Company, in order to further secure the payment of the principal and interest of all of its said General Mortgage Convertible Eight Per Cent Gold Bonds, at any time issued and outstanding under this indenture, accord-

ing to their tenor, purport and effect, and to secure the performance and observance of all of the covenants and conditions therein and herein contained, does hereby agree, for the considerations aforesaid, to deposit with the Trustee and under this indenture to pledge, assign, transfer and set over to the Trustee, and its successors in the trust, and its assigns, such amount of said Series B bonds of the Company (with all interest coupons thereof which are unmatured at the time of such deposit attached) as shall from time to time be necessary in order that there shall be pledged and deposited with the Trustee hereunder one thousand (1,000) dollars principal amount of said Series B bonds for every one thousand (1,000) dollars principal amount of bonds issued hereunder and at the time outstanding, as soon as and when the issuance of said Series B bonds shall be permissible under the provisions of said First and Refunding Mortgage of the Company and the orders of the [fol. 157] Railroad Commission of the State of California, and at all times thereafter while any of the bonds secured hereby shall be outstanding; provided that the lien and claim of the holders of the first $3,500,000 of said bonds upon the first $3,500,000 face value of said Series B bonds of the Company deposited with the Trustee hereunder shall always be prior and superior to the lien and claim thereon of the holders of any of the remaining $1,500,000 of said bonds issued hereunder and the lien and claim of the holders of said remaining $1,500,000 of said bonds upon all of said Series B bonds which shall be pledged hereunder in addition to and after the said $3,500,000 face value of said Series B bonds which shall be first pledged hereunder, shall always be prior and superior to the lien and claim thereon of the holders of said first $3,500,000 of said bonds.

* * * * * * *

Article IV

Redemption and Conversion of Bonds, Sinking Fund and Release

Section 1. At any time when Series B bonds of the Company equal in par value to the par value of the bonds issued hereunder and then outstanding and to the face amount of any outstanding certificates of subscription issued pursuant

to Section 3 of this Article IV, shall be pledged and deposited with the Trustee hereunder, the Company may, at its option, redeem on any interest payment date, at the price [fol. 158] of 105 together with accrued interest, all (but not less than all) of the bonds issued hereunder and then outstanding.

Section 2. The Company covenants that on the 1st day of August during each of the years from 1922 to 1930 inclusive, it will retire, at the price of 105 together with accrued interest, through the operation of the sinking fund provided for in Section 6 of this Article IV, and in the manner herein provided, bonds issued hereunder and then outstanding. Such redemption shall be by lot in each of the years 1922 to 1929, both inclusive, and in the year 1930 shall include all bonds issued hereunder and then outstanding, it being the intention of this indenture that all of the bonds issued hereunder, (excepting only those voluntarily exchanged at the price of 102½ by the holders thereof for Series B bonds of the Company as provided in Section 5 of this Article) shall be retired by the Company at said price of 105 and accrued interest. If there be bonds of both series outstanding hereunder on any such first day of August, the Company shall then retire bonds of each series in the same proportion as the aggregate face amount of the bonds of such series then outstanding bears to the aggregate face amount of the bonds of both series then outstanding hereunder.

Section 3. The holders of any and all bonds called for redemption shall have the option (to be exercised not later [fol. 159] than the redemption date thereof) either of receiving payment for such bonds in cash at said price of 105 together with accrued interest, or of receiving for such bonds Series B bonds of the Company (with the coupon maturing on the interest payment date next following the redemption date and all subsequent coupons attached) equal in par value to the par value of the said bonds so called for redemption, and a premium in cash of five per cent of the face value thereof and interest thereon to date of redemption. The payment of such premium of five per cent shall be made in cash at the office of the Trustee or Co-Trustee. To effect such conversion of bonds issued hereunder into said Series B bonds of the Company, the bondholder shall file

with the Trustee or Co-Trustee not later than the redemption date of the bond to be converted, a written request and agreement for such conversion, and if the same be not so filed with the Trustee or Co-Trustee within such time, the bondholder shall be conclusively deemed to have elected not to exercise his conversion right; provided, however, that in lieu of such request and agreement, the Trustee, at its option, or the Co-Trustee, at its option, may accept the verbal request of any bondholder for conversion, made to it on or prior to such redemption date, accompanied by the delivery to it of the bonds to be converted. In the event that any bond issued hereunder shall be called for redemp- [fol. 160] tion pursuant to Section 2 of this Article at a time when there shall not be sufficient of said Series B bonds deposited with the Trustee hereunder and available for such purpose to effect the conversion of all called bonds, request for the conversion of which shall have theretofore been made to the Trustee or Co-Trustee, as herein provided, and the holder of such bond shall elect to convert the same as herein provided, after sufficient elections shall have been so made to exhaust all said Series B bonds then available for such conversion, the holder of such bond so called for redemption and not then so converted, shall be entitled to receive therefor a sum equal to 105% of the par value of such bond, together with accrued interest thereon, and a certificate in form satisfactory to the Trustee evidencing the right of such bondholder to subscribe at par and accrued interest for the same face amount of Series B bonds of the Company, if and when there shall be deposited with the Trustee and available for that purpose sufficient of said Series B bonds to permit of such conversion; and in such case, when and as additional Series B bonds are so deposited, the holders of subscription certificates shall be permitted to exercise such subscription rights in the order in which they shall elect to make conversion as hereinabove provided. All moneys received by the Trustee as a result of the exercise of such subscription rights shall be immediately paid to the Company. The first [fol. 161] $3,500,000 of Series B bonds pledged hereunder shall be available for conversion only into the first $3,500,000 of said bonds issued hereunder, and any additional Series B bonds so pledged shall be available for conversion

only into the remaining $1,500,000 of said bonds issued hereunder. The Company covenants that it will deposit with the Trustee Series B bonds of the Company equal in face amount to the face amount of all subscription certificates outstanding, as soon as it can lawfully do so under the provisions of said First and Refunding Mortgage and the laws of the State of California.

Said certificates shall be registered by the Trustee, as nearly as practicable in the order in which such elections for conversion shall have been made by said bondholders, and from time to time as Series B bonds available for delivery to certificate holders shall be delivered to the Trustee, the Trustee shall mail notice thereof to holders of outstanding certificates, in the order of registration, equal in face amount to the face amount of the said Series B bonds so on deposit and available for said purpose, at their addresses, if any, left by said certificate holders with said Trustee. If no such address shall have been left with the Trustee, said notice shall be mailed by the Trustee to the person to whom such certificate was issued, addressed to him at the City of New York, New York, and also at San Francisco, California. In the event that the holder [fol. 162] of any certificate shall have assigned the same, and the assignee shall have notified the Trustee in writing of such assignment, together with his address, then and in that event the notice herein provided to be mailed by the Trustee shall be mailed to such assignee at the address so designated by him to the Trustee; but if the assignee of any certificate shall have failed to so notify the Trustee of such assignment, and of his address, as aforesaid, prior to the mailing of such notice, the Trustee shall not be required to give any notice to him. The right of the certificate holder to subscribe for such Series B bonds shall terminate upon the expiration of thirty days after the mailing of such notice by the Trustee, but at any time after the mailing of such notice and prior to the expiration of said period of thirty days he shall be entitled to subscribe for Series B bonds of the Company, as herein provided; provided that in no event shall any of said subscription rights be exercisable after the first day of August, 1930, or after all of the bonds issued hereunder have been redeemed pursuant to this Article IV.

[fol. 163] EXHIBIT C, ANNEXED TO FOREGOING STIPULATION OF FACTS

General Lien Indenture

Dated February 1, 1921

(Condensed)

This exhibit consists of a printed trust indenture between Great Western Power Company of California (therein called the "Company") and the Equitable Trust Company of New York and Anglo-California Trust Company (called the "Trustee" and Co-Trustee', respectively), whereby the Company conveyed and mortgaged its assets and properties, subject to prior encumbrances, in trust for the benefit and security of the holders of its General Lien Convertible Eight Per Cent. Gold Bonds to be issued thereunder. Provision was also made to deposit and pledge with the Trustee, as additional security, a portion of the First and Refunding Mortgage Sinking Fund Gold Bonds of the Company known as its "Series B 7%" bonds. The indenture contains detailed recitals relative to the due authorization and issuance of the Series B 7's and the General Lien 8's, and sets forth a form of bond for the General Lien 8's. This form of bond includes, among other provisions, the following:

"This bond is subject to call and redemption at the office of said Trustee in the City of New York on any interest payment date, after 60 days' published notice, at 105 per cent. of its face value, with accrued interest, in the manner and upon the terms provided in said trust indenture. The [fol. 164] bonds of said issue are convertible into Great Western Power Company of California Series B First and Refunding Mortgage Seven Per Cent. Sinking Fund Gold Bonds, due August 1, 1950, in the manner and subject to the conditions in said trust indenture provided."

The description of properties conveyed and mortgaged includes the following:

"All Series B bonds which may hereafter from time to time be deposited and pledged with the Trustee pursuant to the provisions of this indenture."

The indenture also contains various covenants, conditions and provisions defining the duties, rights and remedies of the Company and of the trustees and bondholders, including the following:

"[Art. I, Sec. 1] The amount of bonds hereby secured is limited, so that there shall never at any time be outstanding bonds of the aggregate principal amount of more than five million (5,000,000) dollars. Said bonds shall be issued in series from time to time as the board of directors of the Company shall determine, and each series shall be distinguished from every other series by some appropriate designation on the face thereof as may be ordered by said board of directors. The first series to be issued hereunder shall be designated 'Series A,' and shall consist of $2,500,000 [fol. 165] principal amount of said bonds, being 250 bonds of the face value of $100 each, numbered from C 1 to C 250; 500 bonds of the face value of $500 each, numbered consecutively from D 1 to D 500, and 2225 bonds of the face value of $1,000 each, numbered consecutively from M 1 to M 2225. * * *"

"[Art. II, Sec. 1] Said $2,500,000 principal amount of said bonds constituting all of the bonds of said Series A, shall forthwith upon the execution and delivery of this trust indenture be authenticated by the Co-Trustee (without awaiting the delivery of any of said Series B bonds to the Trustee), and delivered to the Company upon the written order of the president or a vice-president and the secretary or an assistant secretary of the Company."

"[Art. II, Sec. 2] All Series B bonds of the Company delivered to the Trustee for deposit under this indenture shall be permanent lithographed or engraved bonds in coupon form with all interest coupons thereof which are unmatured at the time of such deposit, attached, and all such bonds shall be lawfully issued under said First and Refunding Mortgage of the Company, shall be dated August 1, 1920, and mature August 1, 1950, and bear interest at the rate of seven (7) per cent. per annum, payable semi-annually on the first day of February and the first day of August of each year, and be redeemable at the option of the Company on any interest date on 60 days' published [fol. 166] notice upon payment of the principal and accrued interest, and if redeemed on or before August 1, 1930, a

premium of ten per cent. of the principal, and if redeemed after August 1, 1930, a premium of one one-half of one per cent. of the principal for each full year of the unexpired term of said bonds; provided, however, that said bonds so to be delivered to the Trustee shall be in denominations of $100, $500 and/or $1,000 as shall from time to time be requested by the Trustee and required for the purpose of conversion into bonds issued hereunder."

"[Art. III, Sec. 1] The Company covenants and agrees that it will duly and punctually pay or cause to be paid the principal and interest of every bond issued hereunder at the times and places and in the manner mentioned in said bonds and in the coupons thereto belonging respectively, according to the true intent and meaning thereof and of these presents."

"[Art. III, Sec. 4] The Company further covenants and agrees that as rapidly as it can lawfully do so under the provisions of said First and Refunding Mortgage and the laws of the State of California, it will deposit and pledge with the Trustee hereunder such amount of said Series B bonds of the Company (with all interest coupons thereof which are unmatured at the time of such deposit attached) as shall from time to time be necessary in order to bring [fol. 167] about as promptly as permitted by said First and Refunding Mortgage and the laws of the State of California the pledge and deposit with the Trustee hereunder of an amount of said Series B bonds equal in par value to the bonds issued hereunder and at the time outstanding."

"[Art. IV] Redemption and Conversion of Bonds * * *.

Section 1. At any time when Series B bonds of the Company equal in par value to the par value of the bonds issued hereunder and then outstanding, shall be pledged and deposited with the Trustee hereunder, the Company may, at its option, redeem on any interest payment date, at the price of 105 together with accrued interest, all or any of the bonds issued hereunder and then outstanding; provided that in the case of redemption of a part only of said bonds, the particular bonds to be redeemed shall be selected by the Trustee by lot in such manner as it may deem proper. In the event that the company elects at any time to redeem

less than all of the bonds issued hereunder and then outstanding, it may designate one or more series from which such redemption shall be made, together with the face amount of bonds to be redeemed in each series.

Section 2. The holders of any and all bonds called for redemption shall have the option (to be exercised not later than the redemption date thereof) either of receiving pay-
[fol. 168] ment for such bonds in cash at said price of 105 together with accrued interest, or of receiving for such bonds Series B bonds of the Company (with the coupon maturing on the interest payment date next following the redemption date and all subsequent coupons attached) equal in par value to the par value of the said bonds so called for redemption, and a premium in cash of five per cent. of the face value thereof and interest thereon to date of redemption. The payment of such premium of five per cent. shall be made in cash at the office of the Trustee or Co-Trustee. To effect such conversion of bonds issued hereunder into said Series B bonds of the Company, the bondholder shall file with the Trustee or Co-Trustee not later than the redemption date of the bond to be converted, a written request and agreement for such conversion, and if the same be not so filed with the Trustee or Co-Trustee within such time, the bondholder shall be conclusively deemed to have elected not to exercise his conversion right; provided, however, that in lieu of such request and agreement, the Trustee, at its option, or the Co-Trustee, at its option, may accept the verbal request of any bondholder for conversion, made to it on or prior to such redemption date, accompanied by the delivery to it of the bonds to be converted.

Section 3. Notices of all calls of bonds for redemption pursuant to the provisions of this Article IV shall be pub-
[fol. 169] lished at least once a week for four successive weeks in a newspaper of general circulation published in said City of New York, and also in a newspaper of general circulation published in said City of San Francisco, the first publication to be not more than 90 days nor less than 60 days prior to the date of redemption. Such notices shall state the numbers of the bonds to be redeemed, if the call be for less than all of the bonds outstanding, the place for redemption, namely, the principal office of the Trustee, in

the City of New York, and also that the holders of such bonds shall be entitled to convert the same into Series B bonds of the Company subject to the conditions of this indenture, on the basis of 105 for the bonds to be redeemed and par for said Series B bonds. If any of the bonds to be redeemed shall be registered, similar notices directed to all of the persons severally who shall appear on the books of the Trustee or Co-Trustee as the registered holders of such bonds, at their addresses as the same shall appear, if at all, on the bond register, shall be mailed, postage prepaid, at least 30 days prior to the date for such redemption. All notices of redemption shall be given by the Company. If on or before such redemption date the Company shall deposit with the Trustees a sum sufficient for the redemption of the bonds that shall have been called for redemption in such published notice. Such bonds so called for redemption shall be from and after the date so set for redemption considered redeemed, and (provided the holder [fol. 170] thereof shall not have elected to convert the same into Series B bonds of the Company as hereinabove provided) they shall become and be payable at the redemption date specified in such notice, at the office of the Trustee, at the principal amount thereof, together with accrued interest due thereon, to such date, and a premium of five per cent. upon the principal. The Company covenants that prior to the redemption date specified in such notice, it will deposit in cash with the Trustee an amount of money sufficient to redeem all of the bonds so called for redemption and which the holder thereof shall not have elected to convert into said Series B bonds as herein provided. On and after the redemption date specified in such notice, the Trustee will take up and pay out of the moneys which shall be deposited with it for that purpose, the bonds which shall have been specified in such notice as called for redemption and which the holder thereof shall not have elected to convert as aforesaid, and said premium thereon and the coupons maturing on the redemption date. Such payment by the Trustee of the sum payable for principal and for premium on each bond called for redemption shall be made to the bearer of such bond unless it shall be registered, in which case such payment shall be made to the registered holder or his assigns, but in either case only upon the surrender of such bonds and all coupons for interest thereon

unmatured at the date of redemption specified in the pub-
[fol. 171] lished notice. All unpaid interest installments represented by coupons which shall have matured on or before the date of redemption specified in the notice shall continue to be payable to the bearers severally and respectively. On and after the redemption date when any bonds called for redemption become payable as aforesaid, the money applicable as aforesaid to the payment and redemption thereof shall be held by the Trustee upon said trust for the payment of such bonds in the manner and at the rate specified; and from and after such redemption date, if the moneys sufficient for such redemption shall have been deposited, no further interest shall accrue upon any such bonds, and any coupon appertaining to such bonds for interest maturing after such date shall become and be null and void; anything in such bonds or in such coupons or in this indenture to the contrary notwithstanding.

* * * * * * *

Section 5. In case the holder of any bond or coupon shall not, within six years after the date fixed as in this Article provided for the redemption of such bond, or of the bond to which such coupon shall appertain, demand payment of the amount deposited as in this Article provided, for the payment of such bond or coupon, the Trustee shall, upon the demand of the Company, its successors or assigns, pay over the amount so deposited for the payment of such bond or
[fol. 172] coupon to the Company, its successors or assigns, and all liability of the Trustees, or either of them, with reference to such money shall thereupon cease.

Section 6. On or after any redemption date there shall be on deposit with the Trustee hereunder Series B bonds equal in principal amount to the amount of bonds issued and outstanding hereunder, the Trustee on the redemption of less than all bonds issued hereunder and outstanding, shall, if there shall not then be any existing default known to the Trustee in the payment of the interest or principal of any of the bonds, or otherwise in the performance of any of the agreements on the part of the Company in the bonds or this indenture contained, assign and deliver to or upon the order of the Company pledged Series B bonds of the Company (constituting part of the Series B bonds upon which the said bonds so redeemed shall be a prior and superior

lien as provided in Section 1 of Article I hereof) to an amount which shall equal in principal amount the bonds so redeemed as herein provided; provided, however, that in no event shall any of said Series B bonds be withdrawn by, or assigned or delivered to the Company, under the provisions of this Section 7, if after such withdrawal, assignment or delivery thereof, the amount par value of said Series B bonds pledged hereunder would be less than the amount par value of bonds issued hereunder and then outstanding.

[fol. 173] Section 7. If by reason of the election of holders of any of said bonds called for redemption to convert the same into Series B bonds of the Company, as hereinabove provided, there shall remain in the hands of the Trustee any money deposited in any year by the Company for the redemption of bonds but not required for that purpose during such year, the same shall be repaid to the Company by the Trustee on the day next following such redemption date.

Section 8. Upon the redemption or conversion of any bond or bonds issued hereunder being effected pursuant to the provisions of this Article, the Trustee shall immediately cancel such bond or bonds, together with all unmatured coupons thereon.

Section 9. The holders of any of the bonds issued hereunder and outstanding on the first day of February, 1935, shall be entitled, at their option, to exchange such bonds (with the coupons maturing on August 1, 1935, and subsequent coupons attached) for Series B bonds of the Company (with the coupons maturing on August 1, 1935, and all subsequent coupons attached) equal in par value to the par value of the bonds issued hereunder and desired to be so exchanged. To effect such conversion of bonds issued hereunder into Series B bonds of the Company, the bondholder shall deliver to the Trustee or Co-Trustee not later than [fol. 174] said first day of Febuary, 1935, a written request for such conversion together with the bonds issued hereunder and desired to be so converted, and if said request and said bonds be not so delivered to the Trustee or Co-Trustee within such time, the bond holder shall be conclusively deemed to have elected not to exercise his conversion rights; provided, however, that in lieu of such request, the Trustee at its option, or the Co-Trustee at its option, may accept the written or verbal request of any bondholder for

conversion, made to it on or prior to the first day of February, 1935, accompanied by the delivery to it of the bonds to be converted."

"[Art. V] Control of Pledged Bonds.

Section 1. The Trustee is authorized in its discretion to hold any and all bonds which it shall receive as security under any of the provisions of this indenture as bearer bonds, or to cause the same to be registered in its name as Trustee.

Section 2. The Trustee, except as herein otherwise expressly provided, shall, as such Trustee, so long as it shall continue to hold hereunder any of said Series B bonds, be considered and held to be the legal owner and holder of said bonds and the accompanying coupons, and, for the purposes of the trust and security herein provided, shall have and in [fol. 175] its discretion may exercise all of the rights and powers of an owner and holder of said bonds and coupons, or any thereof, and under the mortgage securing the same, which a bona fide purchaser thereof for value before maturity would possess or could take; and upon the written request of the holders of twenty-five per cent in amount of the bonds at the time outstanding hereunder, and upon being furnished with reasonable indemnity as hereinafter provided, the Trustee shall exercise any and all such rights and powers so possessed by it and shall, being first so indemnified, take such proper action or proceedings, whether by action at law or suit in equity or otherwise, to that end as shall be so requested by said bondholders. Any proceeds of the property covered by the mortgage and deed of trust securing said bonds that may be received by the Trustee shall be held and applied by it in the same way as if such proceeds were the proceeds of said bonds as provided in Section 6 of Article VI hereof.

Section 3. Unless an 'event of default' as defined in Article VI hereof shall have happened and shall not have been remedied or waived as provided in said Article, the Trustee shall, as they mature, cancel and, upon its written demand, deliver to the Company without the payment thereof, the coupons on all of the pledged Series B bonds held by the Trustee hereunder."

[fol. 176] "[Art. VI, Sec. 2]. If one or more of the events of default shall happen, then and in every such case the

Trustee, either personally or by its attorneys or agents, may, in its discretion, and shall, at the request of the holders of twenty-five (25) per cent in amount of the bonds then outstanding, upon being reasonably indemnified, as hereinafter provided, forthwith proceed, with or without notice to the Company, as in its unqualified discretion the Trustee may determine, and, if upon notice, then upon such notice as in its like discretion the Trustee may give, to sell and convert into money all or any part or parts of the bonds and any other property constituting the trust estate, according to its judgment and discretion, selling the same at one time or from time to time and in each instance either in their entirety or in one or more lots or parcels; provided, however, that the Series B bonds pledged hereunder shall be so sold by the Trustee prior to the sale of the real property mortgaged hereunder";

"[Art. VII, Sec. 1]. The Trustee may, if it deems it advisable, delegate to the Co-Trustee the performance of any duties in this indenture imposed upon the Trustee relative to the conversion of the bonds issued hereunder into Series B bonds of the Company; and the Trustee shall arrange, as far as may be practicable, so that holders of any of the bonds issued hereunder who may be entitled to convert [fol. 177] their said bonds, as aforesaid, and who may desire to effect such conversion at the office of the Co-Trustee, rather than at the office of the Trustee, may do so."

EXHIBIT D, ANNEXED TO FOREGOING STIPULATION OF FACTS

Resolutions of May 8, 1924

(In full except certification)

Whereas, $2,500,000 in aggregate par value, and no more, of the General Lien Convertible Eight Per Cent Gold Bonds of this corporation, Great Western Power Company of Californit issued under the Trust Indenture, dated February 1, 1921, made by this corporation to The Equitable Trust Company of New York, Trustee, and Anglo-California Trust Company, Co-Trustee, to secure an authorized issue of $5,000,000 in aggregate par value of said Bonds, are now outstanding; and

Whereas, Series B First and Refunding Mortgage Sinking Fund Gold Bonds of this corporation equal in par value to the par value of said General Lien Convertible Eight Per Cent Gold Bonds issued under said Trust Indenture and now outstanding, are pledged and deposited with the Trustee under said Trust Indenture;

[fol. 178] Resolved, that all General Lien Convertible Eight Per Cent Gold Bonds of this corporation issued under the Trust Indenture, dated February 1, 1921, made by this corporation, to The Equitable Trust Company of New York, Trustee, and Anglo-California Trust Company, Co-Trustee, to secure an authorized issue of $5,000,000 in aggregate par value of said Bonds, and now outstanding, be, and the same hereby are, called for redemption, and will be redeemed, at the price of 105 together with accrued interest, as provided in and by said Trust Indenture, on August 1, 1924, at the principal office of The Equitable Trust Company of New York, Trustee, in the City of New York, as provided in and by said Trust Indenture;

Further Resolved, that the Secretary of this corporation be, and he hereby is, directed to give notice of said call of said bonds for redemption in the manner and for the time provided in and by said Trust Indenture.

[fol. 179] Exhibit E, Annexed to Foregoing Stipulation of Facts

Railroad Commission Opinion and Order

Dated May 27, 1925

(In Full Except Signatures and Certification)

Decision No. 14979

Before the Railroad Commission of the State of California

Application No. 11111

In the Matter of the Application of Great Western Power Company of California for authority to issue and sell $7,000,000.00 face amount of Series "D" first and refunding mortgage bonds

Guy C. Earl and Chaffee E. Hall, by Chaffee E. Hall, for Applicant

DECOTO, Commissioner:

Opinion

In this application Great Western Power Company of California asks permission to issue and sell, at 94 per cent of face value plus accrued interest, $7,000,000.00 of its Series "D" first and refunding mortgage 5½ per cent bonds due February 1, 1955, and to use the proceeds to refund outstanding seven per cent first and refunding bonds.

[fol. 180] As of December 31, 1924, applicant reported its outstanding bonded indebtedness as follows:

First and refunding bonds:		
Series "A" 6's due 1949	$6,000,000	
Series "B" 7's due 1950	7,535,300	
Series "C" 6's due 1952	6,000,000	$19,535,300
Great Western Power 5's due 1946		20,135,000
City Electric 5's due 1937		1,161,000
Consolidated Electric 5's due 1955		1,540,950
Central Oakland Light & Power 5's due 1939		43,000
Consumer's Light & Power 6's due 1933		68,000
Debentures, 6's due 1925		4,177,600
Total		$46,665,850

Of the $7,535,300.00 of Series "B" first and refunding mortgage bonds, $212,000.00 are held by Western Power Corporation, $112,700.00 are alive in the sinking fund and $7,210,600 are outstanding in the hands of the public. It appears that applicant proposes to purchase the $212,000 of bonds from Western Power Corporation for $218,300, the price paid by Western Power Corporation, and to call the remaining $7,323,300 for redemption on August 1, 1925 at 110, a price requiring the expenditure of $8,055,630. Adding the $8,055,630 to the $218,300 results in a total of $8,273,930 which represents the amount of cash necessary to redeem the outstanding $7,535,300 of Series "B" bonds.

[fol. 181] The company has entered into agreements for the sale of $7,000,000 of the Series "D" bonds at 94, netting $6,580,000. Deducting the $6,580,000 from the total cash requirement of $8,273,930 leaves a balance of $1,693,930. It is of record that the $1,693,930 will be withdrawn from the company's treasury and that such moneys were not obtained from the sale of stock or bonds. It was suggested that at a later date, the company may file an application for permission to issue stock or bonds to reimburse its treasury on account of the withdrawal of $1,693,930. Whether such reimbursement should be allowed will be determined at the time an application is filed for permission to issue stock and bonds for such purpose.

I herewith submit the following form of order:

Order

Great Western Power Company of California having applied to the Railroad Commission for permission to issue and sell $7,000,000 of bonds, a public hearing having been held and the Railroad Commission being of the opinion that the money, property or labor to be procured or paid for through such issue and sale of bonds, is reasonably required for the purpose specified herein, and that the expenditures for such purpose are not in whole or in part reasonably chargeable to operating expense or to income.

It is hereby ordered that Great Western Power Company [fol. 182] of California be and it hereby is, authorized to issue and sell on or before October 1, 1925 at not less than 94 per cent of their face value plus accrued interest $7,000,000 of its Series "D" first and refunding mortgage 5½ per cent bonds due February 1, 1955, and to use the proceeds other than accrued interest to refund in part the outstanding $7,535,300.00 of Series "B" first and refunding mortgage seven per cent bonds to which reference is made in the foregoing opinion. The accrued interest may be used for general corporate purposes.

The authority herein granted is subject to further conditions as follows:

1. Applicant shall keep such record of the issue, sale and delivery of the bonds herein authorized and of the disposition of the proceeds as will enable it to file on or before the 25th day of each month a verified report, as required

by the Railroad Commission's General Order No. 24; which order in so far as applicable, is made a part of this order.

2. The authority herein granted shall become effective upon the date hereof.

The foregoing Opinion and Order are hereby approved and ordered filed as the Opinion and Order of the Railroad Commission of the State of California.

Dated at San Francisco, California, this 27th day of May, 1925.

[fol. 183] EXHIBIT F, ANNEXED TO FOREGOING STIPULATION OF FACTS

Railroad Commission Opinion and Order

Dated February 5, 1925

(In full Except Signatures)

Decision No. 14541

BEFORE THE RAILROAD COMMISSION OF THE STATE OF CALIFORNIA

Application No. 10785

In the Matter of the Application of GREAT WESTERN POWER COMPANY OF CALIFORNIA, a corporation, to issue and sell $1,500,000.00 of Series "D" first and refunding mortgage bonds and $2,000,000.00 of Preferred Stock

CHAFFEE E. HALL, for Applicant.

SQUIRES, Commissioner:

Opinion

Great Western Power Company of California asks permission to issue and sell at 92½% of their face value and accrued interest, $1,500,000.00 of its Series "D" 5½% 30 year first and refunding mortgage bonds to be dated February 1st, 1925; and to issue and sell at not less than 95% of par value, net, $2,000,000 par value of its 7% cumula-

tive preferred stock. It further asks permission to use [fol. 184] $502,914.17 of the net proceeds obtained from the sale of the bonds and preferred stock to reimburse its treasury because of income expended for the acquisition of property and for the construction, completion, extension and improvement of its facilities described in applicant's Exhibits "A" and "B" and use the remainder of the net proceeds (not less than $2,784,585.83) for the acquisition of property and for the construction, completion, extension and improvement of facilities described in applicant's Exhibits "C" and "D."

The Company reports that it will sell the $1,500,000.00 of bonds subject to their issue being authorized by the Commission, to E. H. Rollins and Sons at 92½% and accrued interest. A copy of the agreement between applicant and E. H. Rollins and Sons has been filed in this proceeding as Applicant's Exhibit "E." The agreement shows that the bonds are to be dated February 1st, 1925, to mature in thirty years and to bear interest at the rate of 5½% per annum. It further shows that the bonds are to be callable in whole or in part on the first day of any month on 60 days' notice at 102½% for the first ten years and thereafter at a premium of ⅛% for each year or fraction thereof of the unexpired term.

It is of record that the Company has entered into no underwriting agreement covering the sale of the $2,000,000.00 of 7% cumulative preferred stock. The sale of this stock will be handled in the same manner as the sale of stock by applicant heretofore. It is the intention to offer the stock for sale at par. Applicant asks permission to ex- [fol. 185] pend of the proceeds for the payment of commissions and expenses incident to the sale of the stock an amount not exceeding five per cent of the par value of the stock sold. It may be that the expenses including the commissions will be less than five per cent.

The Company reports in its Exhibit "A" that up to December 31st, 1924 it has expended for capital purposes the sum of $502,914.17 against which the Commission has not authorized the issue of any stock or bonds. Because of this expenditure, it asks permission to reimburse its treasury in such amount through the use of proceeds obtained from the sale of the $1,500,000.00 of bonds and the $2,000,000 of 7% preferred stock. The Company estimates

its construction expenses (Exhibits "C" and "D") for 1925 at $2,846,321.00. These expenses are summarized as follows:

Production Capital:		$94,813.
Big Meadows-surveys and dredging	$54,360.	
Big Bend-gear pumps and governor for oil supply	13,053.	
Caribon-Club house	25,000.	
North Beach-boiler breaching and flue	2,400.	
Transmission Capital:		369,587.
Sacramento	15,930.	
Oakland	349,407.	
Arboga	3,000.	
Antioch	1,250.	
[fol. 186] Distribution Capital:		796,921.
Sacramento	39,200.	
Northwestern	3,000.	
Oakland	368,406.	
San Francisco	246,078.	
Mapa	84,919.	
Potaluma	24,918.	
Santa Rosa	24,583.	
Steam Heat	5,817.	
Distribution Line Extensions General Capital:		1,500,000.
San Francisco Division	$545,000.	
Northwestern Division	95,000.	
Oakland Division	515,000.	
Sacramento Division	315,000.	
Big Meadows Division	30,000.	
General Capital:		85,000.
Butt Valley Roads	10,000.	
Sutter Street Office Building	35,000.	
Sacramento Service Building	40,000.	
Total		$2,846,321.

If the Company's $1,500,000 of bonds and $2,000,000 of stock are sold at the net prices indicated herein, it will

realize the sum of $3,287,500. The construction expenditures, which have not heretofore been financed through the [fol. 187] issue of bonds and stock, and the estimated expenditures for 1925 amount to $3,349,235.17.

I herewith submit the following form of order:

Order

Great Western Power Company of California having applied to the Railroad Commission for permission to issue and sell $1,500,000 of bonds and $2,000,000 of 7% cumulative preferred stock, a public hearing having been held, and the Railroad Commission being of the opinion that the money, property or labor to be procured or paid for through the issue of such stock and bonds is reasonably required by applicant and that the expenditures herein authorized are not in whole or in part reasonably chargeable to operating expenses or income.

It is hereby ordered that the Great Western Power Company of California be, and it is hereby authorized to issue, sell and deliver, on or before May 1st, 1925, at not less than 92½% of their face value, $1,500,000 of its Series "B" 5½% 30 year first and refunding mortgage bonds to be dated February 1st, 1925.

It is hereby further ordered that the Great Western Power Company of California be, and is hereby, authorized to issue, sell and deliver, on or before December 31st, 1925, at not less than 95% of par value, net to applicant $2,000,000 par value of its 7% cumulative preferred stock.

The authority herein granted is subject to further conditions as follows:

[fol. 188] 1. Of the net proceeds realized from the sale of the bonds and preferred stock, $502,914.17 may be used by applicant to reimburse its treasury because of income expended for the acquisition of properties, and for the construction, completion, extension and improvement of its facilities described in applicant's Exhibit "A" and Exhibit "B" provided only such costs as are properly chargeable to fixed capital accounts under the uniform system of accounts prescribed by the Railroad Commission may be financed through the use of the $502,914.17.

2. The remainder of the net proceeds obtained from the sale of the bonds and stock herein authorized to be issued and sold may be used by applicant to finance such portion of the cost of the additions and betterments described in Exhibit "C" and Exhibit "D" filed in this proceeding as is properly chargeable to fixed capital accounts under the uniform system of accounts as prescribed by the Commission.

3. Applicant shall keep such record of the issue, sale and delivery of the bonds and stock herein authorized and of the disposition of the proceeds as will enable it to file, on or before the 25th day of each month, a verified report as required by the Railroad Commission's General Order No. 24, which order, in so far as applicable, is made a part of this Order.

[fol. 189] 4. The authority herein granted to issue and sell stock will become effective upon the date hereof. The authority herein granted to issue and sell bonds will become effective when applicant has paid the fee prescribed by Section 57 of the Public Utilities Act, which fee is $1,250.00.

The foregoing opinion and order are hereby approved and ordered filed as the Opinion and Order of the Railroad Commission of the State of California.

Dated at San Francisco, California, this 5th day of February, 1925.

[fol. 190] EXHIBIT G, ANNEXED TO FOREGOING STIPULATION OF FACTS

Railroad Commission Opinion and Order

Dated October 21, 1925

(In Full Except Signatures)

Decision No. 15544

BEFORE THE RAILROAD COMMISSION OF THE STATE OF CALIFORNIA

Application No. 11759

In the Matter of the Application of GREAT WESTERN POWER COMPANY OF CALIFORNIA for authority to issue and sell $1,000,000 face amount of Series "D" first and refunding mortgage bonds and $4,000,000 face amount of five year five and one-half per cent notes.

Guy C. Earl and Chaffee E. Hall, by Chaffee E. Hall, for Applicant

DECOTO, Commissioner:

Opinion

In this proceeding Great Western Power Company of California asks permission to issue and sell $1,000,000 of its Series "D" first and refunding mortgage bonds at not [fol. 191] less than 95 per cent of face value, and $4,000,000 of unsecured notes at not less than 95.75 per cent of face value. The company also asks permission to use the proceeds to be obtained from the sale of the bonds and notes, together with the $1,387,500 heretofore obtained from the sale at 92.5 of the $1,500,000 of Series "D" bonds authorized by Decision No. 14541, to reimburse its treasury on account of moneys expended in re-acquiring the company's Series "B" bonds and to provide for the payment at maturity on November 1, 1925 of the $4,177,600 of the ten year six per cent debentures now outstanding.

As of March 1, 1919, applicant executed its first and refunding mortgage. The mortgage is of the "open-end" type. The bonds secured thereby are to be issued in series

of such date, maturity, not later than March 1, 1979, interest rate, redemption and conversion features and of such other provisions as may be determined at the time of issue. Heretofore the company issued $6,000,000 of Series "A" six per cent bonds due 1949, $8,500,000 of Series "B" seven per cent bonds due 1950, $6,000,000 of Series "C" six per cent bonds due 1952 and $8,500,000 of Series "D" five and one-half per cent bonds due 1955.

The company reports that prior to January 1, 1925, it re-acquired $964,700 of the Series "B" bonds at a cost of $1,025,556.75 and on August 1, 1925, it redeemed the remaining $7,535,300 at a cost of $8,273,940 the total cost of re-acquiring the $8,500,000 of Series "B" bonds being $9,299,496.75. Of this amount it is said that $6,978,900 [fol. 192] was provided by the sale of bonds heretofore authorized by the Commission, leaving expenditures of $2,320,596.75 which applicant alleges have not been paid or provided through the issue of stock, bonds or other securities but were made with moneys in the treasury received from other sources.

In addition to these expenditures, it appears that applicant will be required to expend $4,177,600 in paying at maturity on November 1, 1925, the six per cent debentures now outstanding. Adding the $4,177,600 to the $2,320,596.75 results in a total of $6,498,196.75.

To provide in part this amount applicant now asks permission to issue and sell the $1,000,000 of Series "D" bonds and the $4,000,000 of notes. The bonds are identical to the Series "D" bonds now outstanding, are dated February 1, 1925, bear interest at 5½ per cent per annum, mature February 1, 1955, and are callable at a premium of one-eighth of one per cent for each year of the unexpired term.

The notes are a new issue. They will be unsecured, will be dated November 2, 1925, bear interest at 5½ per cent per annum, mature November 2, 1930 and be callable at a premium of one-fourth of one per cent for each year of the unexpired term.

The record shows that applicant has made arrangements to sell the $1,000,000 of bonds at 95 and the $4,000,000 of notes at 95.75, or for a total of $4,780,000. In addition, it now has on hand $1,387,500 which it obtained from the sale, [fol. 193] at 92½, of the $1,500,000 of Series "D" bonds authorized by Decision No. 14541, dated February 5, 1925, in Application No. 10786. The total proceeds on hand and

to be received thus amount to $6,167,500. Deducting the $4,177,600 needed to retire the debentures leaves a balance of $1,989,900 available for reimbursement. In this connection, James B. Black, applicant's vice-president, and general manager, testified that after reimbursement the proceeds would be used for construction purposes. The construction program of the company has been outlined in former proceedings.

I herewith submit the following form of order:

Order

Great Western Power Company of California, having applied to the Railroad Commission for permission to issue bonds and notes, a public hearing having been held and the Railroad Commission being of the opinion that the money, property or labor to be procured or paid for through such issue and sale is reasonably required by applicant for the purposes specified herein and that the expenditures are not in whole or in part reasonably chargeable to operating expense or to income.

It is hereby ordered that Great Western Power Company of California be, and it is hereby, authorized to issue and sell at not less than 95 percent of face value plus accrued interest, $1,000,000 of its Series "D" first and refunding [fol. 194] bonds, and at not less than 95.75 percent of face value plus accrued interest, $4,000,000 of five year five and one half percent unsecured notes.

It is hereby further ordered that Great Western Power Company of California be, and it is hereby, authorized to use the proceeds, other than accrued interest, to be received through the issue and sale of the bonds and notes herein authorized, together with the proceeds received from the sale of the $1,500,000 of Series "D" bonds authorized to be issued by Decision No. 14541 dated February 5, 1925, to pay at maturity the $4,177,600 of debentures and to reimburse its treasury on account of moneys expended in retiring its Series "B" first and refunding mortgage bonds; and Decision No. 14541 dated February 5, 1925 be, and it is hereby, modified so as to permit Great Western Power Company of California to use the proceeds from the sale of the Series "D" bonds authorized therein for the purposes mentioned. The accrued interest may be used for general corporate purposes.

The authority herein granted is subject to further conditions as follows:

1. All proceeds used to reimburse applicant's treasury on account of moneys expended to retire Series "B" bonds, shall be used to finance in part construction expenditures.

2. Applicant shall keep such record of the issue, sale and [fol. 195] delivery of the bonds and notes herein authorized to be issued and of the disposition of the proceeds as will enable it to file on or before the 25th day of each month a verified report as required by the Railroad Commission's General Order No. 24, which order in so far as applicable, is made a part of this order.

3. The authority herein granted to issue bonds and notes will become effective when applicant has paid the fee prescribed by Section 57 of the Public Utilities Act, which fee is $1,082.50.

4. Under the authority herein granted no bonds or notes may be issued after December 31, 1925.

The foregoing opinion and order are hereby approved and ordered filed as the Opinion and Order of the Railroad Commission of the State of California.

Dated at San Francisco, California, this 21st day of October, 1925.

[fol. 196] EXHIBIT H, ANNEXED TO FOREGOING STIPULATION OF FACTS

(In Full Except Certification)

Extract from Minutes of a Special Meeting of the Board of Directors of Great Western Power Company of California, held on February 5, 1925

Mr. H. P. Wilson, Vice-President of the Company, then stated that under date of January 22, 1925, acting for and on behalf of this Company, he hade made an agreement in writing with E. H. Rollins & Sons for the sale by this Company, and the purchase by E. H. Rollins & Sons, at the price of 92½ and accrued interest of $1,500,000 face amount of Series D First and Refunding Mortgage Bonds of this

Company. He then produced and read to the Board the said agreement with E. H. Rollins & Sons, and same was ordered spread upon the minutes of this meeting. Said agreement was and is in words and figures, as follows, to-wit:

"E. H. Rollins & Sons, 43 Exchange Place, New York

January 22nd, 1925.

Great Western Power Company of California, San Francisco, California.

DEAR SIR:

We hereby offer to purchase from you $1,500,000 of your [fol. 197] First and Refunding Mortgage 5½% Thirty-Year Sinking Fund Gold Bonds, Series D, to be dated February 1, 1925, at 92½ and accrued interest, subject to the approval of the Railroad Commission of California and to the approval of the legalities by our counsel, payment to be made in New York funds against delivery of the bonds at our New York office in temporary or definitive form on or before April 1, 1925. The Series D bonds are to be issued by you as soon as possible, are to be callable in whole or in part on the first day of any month on sixty days' notice at 102½ for the first ten years and thereafter at a premium of ⅛% for each year or fraction thereof of the unexpired term and are to provide for the usual refunding of taxes to holders resident in Massachusetts and Pennsylvania. Except as required by the foregoing description, the form of the Series D bonds is to be substantially similar to that of your bonds of Series A outstanding under the same mortgage.

Your acceptance of this offer will constitute a contract between us for the purchase of these bonds.

Yours very truly, (Signed) E. H. Rollins & Sons.

Accepted: (Signed) H. P. Wilson, Vice-Pres.
—— —, 1925"

[fol. 198] Thereupon on motion duly made and seconded, the following resolutions were passed and adopted by the vote of Directors Mortimer Fleishhacker, W. H. Spaulding, J. B. Black, Guy C. Earl, E. H. Cox and H. P. Wilson:

Resolved, that the action of H. P. Wilson, Vice-President of this Company, Great Western Power Company of California, in executing and delivering for and on behalf of this Company an agreement in writing dated January 22, 1925 with E. H. Rollins & Sons, a corporation laid before the Board of Directors and spread upon the minutes of this meeting, providing, among other things, for the sale by this Company and the purchase by E. H. Rollins & Sons at the price of 92½ and accrued interest of $1,500,000 face amount of Series D First and Refunding Mortgage Bonds of this Company be, and the same hereby is, ratified, approved and confirmed as the act and deed of this corporation;

Further resolved, that the officers of this Company be, and they hereby are, authorized, empowered and directed to do all things necessary, proper and expedient to carry into effect the purpose of the foregoing resolution and the agreement therein referred to.

Mr. Dibblee, being an officer of E. H. Rollins & Sons, did not vote upon the foregoing resolutions.

The Chairman then called the attention of the Board to the fact that in order to comply with the provisions of the [fol. 199] aforesaid agreement with E. H. Rollins & Sons, it would be necessary to authorize the issuance of a fourth series of bonds to be issued under the Company's First and Refunding Mortgage dated March 1, 1919.

EXHIBIT I, ANNEXED TO FOREGOING STIPULATION OF FACTS

(In Full Except Certification)

Extract from Minutes of a Special Meeting of the Board of Directors of Great Western Power Company of California

Held May 15, 1925

The President then stated that on account of the favorable market for the bonds of this company, it would be to the best interests of the company to retire the outstanding Series B 7% Sinking Fund Bonds of the company by calling the same for redemption at the specified call price of 110, on August 1, 1925. He further stated that there was sufficient cash in the company's treasury, when supple-

mented by the money to be received from the sale of $7,000,000 of Series D First and Refunding Mortgage Bonds, arrangements for which had been made, to finance the redemption.

Thereupon, on motion duly made and seconded, the following resolutions were put two vote and unanimously adopted.

[fol. 200] Resolved, That all of the series of bonds designated as Series B issued under the indenture dated March 1, 1919, made by this corporation, Great Western Power Company of California, to Bankers Trust Company, Trustee, and now outstanding, be and the same hereby are, called for redemption, and will be redeemed at a price equivalent to the principal, accrued interest and a premium of ten per cent. of the principal, on the first day of August, 1925, at the principal office of said Bankers Trust Company, in the City of New York, State of New York, as provided in said bonds and said indenture.

Further resolved, That the Treasurer of this corporation be and he hereby is authorized and directed to deposit with said Bankers Trust Company, Trustee, before said first day of August, 1925, an amount of money sufficient to redeem said bonds to be held for the account of the holders thereof, and to be paid to them respectively upon presentation and surrender of said bonds with all unmatured coupons thereto belonging.

Further resolved, That the Secretary of this corporation be and he hereby is authorized and directed to give on behalf of this corporation notice of intention to redeem said bonds, as provided in said indenture and said bonds.

The Chairman then stated that in order to carry out the financial plans of the company, including the retirement [fol. 201] of the outstanding Series B Bonds, it would be necessary to make provision for the issuance of an additional $9,200,000 face amount of Series D First and Refunding Mortgage Bonds.

Thereupon, on motion duly made and seconded, the following resolutions were put to vote and unanimously adopted:

Whereas, this Corporation has heretofore made provision for the issuance of $1,500,000 in aggregate principal amount

of its First and Refunding Mortgage Sinking Fund Gold Bonds of Series D; and

Whereas, this corporation has obligated itself for a valuable consideration to make provision for the issuance of an additional $9,200,000 in aggregate principal amount of said bonds of Series D.

Now, therefore, be it resolved, that an additional $9,200,000 in aggregate principal amount of said bonds of Series D, being 8,950 bonds for $1,000 each, numbered from M-1425 to M-10372, inclusive; and 500 bonds for $500 each, numbered from D-181 to D-680, inclusive, shall be forthwith executed by the President or any Vice President of this corporation, and impressed with its corporate seal, attested by its Secretary or any Assistant Secretary and delivered to Bankers Trust Company, Trustee, under the First and Refunding Mortgage of this corporation, dated March 1, [fol. 202] 1919, to be held by said Trustee until it shall be required to certify and deliver the same from time to time to this corporation or upon its order, as provided in Article II of said Mortgage.

The Chairman then laid before the Board a certificate dated May 13, 1925, signed by Guy C. Earl, President of this Company, and C. M. Mardel, its Engineer, stating that the Company has within three years prior to the date of said certificate acquired and constructed certain plants, property, permanent improvements, extensions and additions at the expense of $844,490.26; and also a report, dated May 13, 1925, signed by Guy E. Earl, President of this company, and by Haskins & Sells, certified public accountants, setting forth, among other things, the amount of the net earnings of the company and its subsidiaries for the twelve consecutive calendar months ending March 31, 1925; and also an opinion of Guy C. Earl, Esq., attorney at law, dated May 13, 1925, stating, among other things, that the company has title to the plants, property, permanent improvements, extensions and additions described in said certificate; and he called the Board's attention to the fact that it appears from said certificate, said report and said opinion that the company is entitled, under its First and Refunding Mortgage, to call for the certification and delivery by the Trustee under said mortgage of more than $700,000 face amount of Series D Bonds.

Thereupon, on motion duly made and seconded, the following resolutions were put to vote and unanimously adopted:

[fol. 203] Whereas, Guy C. Earl, President of this corporation, and C. M. Mardel, an engineer appointed by this Board of Directors, have jointly made and signed a certificate, dated May 13, 1925, stating among other things, that this corporation has, within three years prior to the date of said certificate, acquired and constructed certain plants, property, permanent improvements, extensions and additions described in said certificate; and

Whereas, the actual cash cost to the Company of the plants, property, permanent improvements, extensions and additions included and described in said certificate was the sum of $844,490.26; and

Whereas, it appears to this Board of Directors from said certificate and from a report, dated May 13, 1925, signed by Guy C. Earl, President of this corporation, and by Haskins and Sells, certified public accountants (setting forth, among other things, the amount of net earnings of this corporation and of each of its subsidiary companies for the twelve consecutive calendar months ending March 31, 1925), and from an opinion of Guy C. Earl, Esq., attorney at law, counsel selected by this Board of Directors, dated May 13, 1925 (stating among other things, that this corporation has title to said plans, property, permanent improvements, extensions and additions), that this corporation is entitled, under the provisions of Limitation Fifth of [fol. 204] Section 3 of Article II of the First and Refunding Mortgage of this corporation, dated March 1, 1919, to the certification and delivery of First and Refunding Mortgage Sinking Fund Gold Bonds of a face value in excess of $700,000;

Now, therefore, be it resolved, that this corporation, Great Western Power Company of California, a corporation of the state of California, requests and does hereby request, Bankers Trust Company, Trustee under the First and Refunding Mortgage of this corporation, dated March 1, 1919, to certify and deliver to H. P. Wilson, Vice President, and F. M. Tompkins, Treasurer, of this corporation, or upon their order, First and Refunding Mortgage Sinking Fund Gold Bonds of this corporation of the aggregate

principal amount of $700,000 designated Series D, dated February 1, 1925, maturing February 1, 1955, bearing interest at the rate of five and one-half per cent per annum, redeemable at the option of this corporation on any interest date upon sixty days' published notice, upon payment of the principal, accrued interest and if redeemed before the 1st day of February, 1935, a premium of two and one-half per cent of the principal; and if redeemed on or after the 1st day of February, 1935, a premium of one-eighth of one per cent for each year or fraction of a year of the then expired term.

Further resolved, that said bonds shall be 700 in number, [fol. 205] shall be for $1,000 each; and shall be numbered from M-1423 to M-2122, inclusive.

The Chairman then stated that upon the delivery to Bankers Trust Company, as Trustee under this company's First and Refunding Mortgage, of such Series B Bonds as are owned by the company and upon the deposit with said Trustee, before August 1, 1925, of an amount of money equal to the principal, accrued interest and a premium of ten per cent of all of the $8,500,000. in principal amount of such Series B Bonds not so delivered, this company would be entitled, under the provisions of said First and Refunding Mortgage to the certification and delivery by said Trustee of $8,500,000. face amount of Series D First and Refunding Mortgage Bonds.

Thereupon, on motion duly made and seconded, the following resolutions were put to vote and unanimously adopted:

Whereas, there have been issued under the First and Refunding Mortgage of this Corporation, Great Western Power Company of California, dated March 1, 1919, made by this corporation to Bankers Trust Company, as Trustee, to secure the First and Refunding Mortgage Sinking Fund Gold Bonds of this corporation, Eight Million, Five Hundred Thousand Dollars ($8,500,000.), and no more, in aggregate principal amount of a series of bonds designated as Series B, dated August 1, 1920, due Angust 1, 1950, and bearing interest at the rate of seven per cent per annum; and

[fol. 206] Whereas, of said Eight Million, Five Hundred Thousand Dollars ($8,500,000.) in principal amount of

Series B Bonds, a part have been reacquired and are owned by this corporation, a part are held by Bankers Trust Company, as Trustee under said First and Refunding Mortgage, as the property of the Sinking Fund provided for in said First and Refunding Mortgage, and the remainder are outstanding in the hands of the public; and

Whereas, this corporation has called for redemption and intends to redeem all of said Series B Bonds now outstanding at a price equivalent to the principal, accrued interest and a premium of ten per cent of the principal on August 1, 1925, as provided in said First and Refunding Mortgage and said Bonds; and

Whereas, this corporation desires to issue in lieu of said Eight Million, Five Hundred Thousand Dollars ($8,500,000.) principal amount of Series B Bonds, a like principal amount of Series D First and Refunding Mortgage Sinking Fund Gold Bonds of this corporation;

Now, therefore, be it resolved, that this corporation, Great Western Power Company of California, request and does hereby request Bankers Trust Company, as Trustee under said First and Refunding Mortgage of this corporation, to certify and deliver to H. P. Wilson, Vice President, [fol. 207] and F. M. Tompkins, Treasurer of this corporation, or upon their order, First and Refunding Mortgage Sinking Fund Gold Bonds of this corporation of the aggregate principal amount of Eight Million Five Hundred Thousand Dollars ($8,500,000) designated as Series D upon the delivery to said Bankers Trust Company, before August 1, 1925, of such Series B Bonds as may be then owned by this corporation, and upon the deposit with said Bankers Trust Company, as Trustee, before August 1, 1925, of an amount of money equivalent to the principal, accrued interest and a premium of ten per cent of the principal of all of said Eight Million, Five Hundred Thousand Dollars ($8,500,000) in principal amount of said Series B Bonds not so delivered.

Further resolved, that said Series D Bonds shall be dated Feb. 1, 1925, shall mature Feb. 1, 1955, shall bear interest at the rate of five and one-half per cent. (5½%) per annum, shall be redeemable at the option of this corporation on any interest date upon sixty days' published notice, upon payment of the principal, accrued interest and if

redeemed before the 1st day of February, 1935, a premium of two and one-half per cent of the principal, and if redeemed on or after the 1st day of February, 1935, a premium of one-eighth of one per cent. for each year or fraction of a year of the then unexpired term.

Further resolved, that of said Series D Bonds so certified [fol. 208] and delivered, 8,250 shall be for One Thousand Dollars ($1,000) each, numbered from M-2123 to M-10372, inclusive; and 500 shall be for Five Hundred Dollars ($500) each numbered from D-181 to D-680, inclusive.

The Chairman then stated that Mr. H. P. Wilson, Vice President of the Company, acting for and on behalf of this company, had made an agreement in writing dated May 13, 1925, with E. H. Rollins & Sons for the sale by this company, and the purchase by E. H. Rollins & Sons, at the price of 94 and accrued interest of $6,300,000. face amount of Series D First and Refunding Mortgage Bonds of this company. He then produced and read to the Board the said agreement with E. H. Rollins & Sons, and same was ordered spread upon the minutes of this meeting. Said agreement was and is in words and figures as follows, to wit:

May 13, 1925.

Great Western Power Company of California, San Francisco, California.

Dear Sirs:

We hereby offer to purchase from you $6,300,000. of your First and Refunding Mortgage 5½ Thirty Year Sinking Fund Gold Bonds, Series D, which shall be similar in all respects to the Series D Bonds now outstanding at 94 and [fol. 209] accrued interest, subject to the approval of the Railroad Commission of California and to the approval of the legalities by our counsel.

It is understood that you will arrange for the delivery to us of Interim Receipts of the Bank of America which we will take up and pay for on June 10th, 1925, exchangeable for the Definitive bonds when, as, and if issued.

It is understood that all expenses in connection with the issuance of temporary and permanent bonds and interim receipts and fees of our counsel are to be paid by you.

Your acceptance of this offer will constitute a contract between us for the purchase of these bonds.

Very truly yours, E. H. Rollins & Sons.

Accepted: Great Western Power Company of California, H. P. Wilson, Vice President.

—— —, 1925.

HWB/R.

Thereupon, on motion duly made and seconded, the following resolutions were put to vote and unanimously adopted:

Resolved, that the action of H. P. Wilson, Vice-President of this company, Great Western Power Company of California, in executing and delivering for and on behalf of this company, an agreement in writing, dated May 13, 1925, [fol. 210] with E. H. Rollins & Sons, a corporation, laid before the Board of Directors, and spread upon the minutes of this meeting, providing among other things for the sale by this company, and the purchase by E. H. Rollins & Sons, at the price of 94 and accrued interest of $6,300,000 face amount of Series D First and Refunding Mortgage Bonds of this company, be, and the same hereby is, ratified, approved and confirmed as the act and deed of this corporation.

Further resolved, that the officers of this company be and they hereby are authorized, empowered and directed to do all things necessary, proper and expedient to carry into effect the purpose of the foregoing resolution and the agreement therein referred to.

The Chairman then stated that Mr. Wilson, acting for and on behalf of the company, had also agreed to sell to Western Power Corporation, a corporation of New York, $700,000 face amount of said Series D Bonds at 94 and accrued interest.

Thereupon, on motion duly made and seconded, the following resolutions were put to vote and unanimously adopted:

Resolved, that the action of H. P. Wilson, Vice President of this company, Great Western Power Company of California, in agreeing for and on behalf of this company to sell

to Western Power Corporation, a corporation of the State [fol. 211] of New York, at the price of 94 and accrued interest, $700,000 face amount of Series D First and Refunding Mortgage Bonds of this company, be, and the same hereby is, ratified, approved and confirmed as the act and deed of this corporation.

Further resolved, that the officers of this company be and they hereby are authorized, empowered and directed to do all things necessary, proper, and expedient to carry into effect the purpose of the foregoing resolution and the agreement therein referred to.

EXHIBIT J, ANNEXED TO FOREGOING STIPULATION OF FACTS

(In Full Except Certification)

Extract from Minutes of a Special Meeting of the Board of Directors of Great Western Power Company of California, Held on September 25, 1925

The Chairman stated that H. P. Wilson, Vice-President of this Company, acting for and on behalf of the Company, had made an agreement in writing, dated September 23, 1925, with E. H. Rollins & Sons for the sale by this Company and the purchase by E. H. Rollins & Sons at the price of 95 and accrued interest of $1,000,000 face amount of Series D First and Refunding Mortgage Bonds of this Company. He then produced and read to the Board the said agreement [fol. 212] with E. H. Rollins & Sons, and the same was ordered spread upon the minutes of this meeting. Said agreement was and is in words and figures as follows, to wit:

"Mr. H. P. Wilson, Vice President, Great Western Power Company of California, 50 Broad Street, New York City.

DEAR SIR:

Confirming our conversation we offer to purchase from you $1,000,000 par value Great Western Power Company of California First and Refunding Sinking Fund Series D, 5½% Gold Bonds, at a price of 95% of par and accrued in-

terest to date of delivery to us. This offer is subject to the following terms and conditions:

1. We are to sell these bonds at the price of 99% of par, or if we sell them at a higher price are to pay you the difference between the price at 99 and such sale price as we may obtain.

2. Delivery of the bonds is to be made to us in New York City on such date as we shall determine on or before November 2, 1925. It is our understanding that these bonds have been issued under and are now outstanding and secured by the First and Refunding Mortgage of Great Western Power Company of California to Bankers Trust [fol. 213] Company as Trustee, dated March 1, 1919, and constitutes an additional purchase by us of Series D bonds identical with the bonds previously purchased by us and described in the annexed circular. Our obligation to take delivery of these bonds is subject to approval of counsel as to all legal details of the issue of these bonds and their sale by you to us.

3. Your acceptance of the above offer under the terms and conditions as outlined will constitute a contract for the purchase of these bonds.

Yours truly, E. H. Rollins & Sons, by Signed H. W. Briggs.

Accepted this 23d day of September, 1925:

Great Western Power Company of California, by Signed H. P. Wilson, Vice-President."

Thereupon on motion duly made and seconded, the following resolutions were passed and adopted by vote of all of the directors present at the meeting except Mr. Dibblee who, being an officer and director of E. H. Rollins & Sons, had asked to be excused from voting:

Resolved that the action of H. P. Wilson, Vice President of this company, Great Western Power Company of California, in executing and delivering for and on behalf of this [fol. 214] company an agreement in writing, dated September 23, 1925, with E. H. Rollins & Sons, a corporation, laid before this Board of Directors and spread upon the minutes of this meeting, providing, among other things, for the sale

by this company and the purchase by E. H. Rollins & Sons, at the price of 95 and accrued interest, of $1,000,000 face amount of Series D First and Refunding Mortgage Bonds of this company be and the same hereby is ratified, approved and confirmed as the act and deed of this corporation;

Further resolved that the officers of this Company be and they hereby are authorized, empowered and directed to do all things necessary, proper and expedient to carry into effect the purpose of the foregoing resolution and the agreement therein referred to.

Thereupon, counsel for the parties offered a further stipulation of facts, which was duly received in evidence as Stipulation of Facts No. 3, and (omitting the caption and signatures) is in words and figures as follows:

STIPULATION OF FACTS No. 3

It is hereby stipulated and agreed by and between the parties hereto as follows:

1. The consolidated return for the year 1924 in the name of the Western Power Corporation referred to in paragraph 1 of the stipulation of facts filed June 5, 1933, was [fol. 215] filed in the office of the Collector of Internal Revenue for the Second District of New York.

2. The consolidated return for the year 1925 referred to in paragraph 2 of the stipulation of facts filed June 5, 1933, was filed with the Collector of Internal Revenue for the First District of California.

3. The consolidated return for the year 1926 referred to in paragraph 3 of the stipulation of facts filed June 5, 1933, was filed with the Collector of Internal Revenue for the First District of California.

4. In the event it becomes necessary for settlement under Rule 50 in this proceeding, the parties agree, subject to the approval of the Board, that any or all of said returns may then be received in evidence.

Whereupon, after statements of counsel, the proceeding was submitted.

The foregoing is all of the material evidence adduced at the hearing before the United States Board of Tax Appeals, and the same is approved by the undersigned Robert H. Jackson, Assistant General Counsel for the Bureau of Internal Revenue, as attorney for the Commissioner of Internal Revenue.

(Signed) Robert H. Jackson, Assistant General Counsel for the Bureau of Internal Revenue.

[fol. 216] The foregoing is all of the material evidence adduced at the hearing before the United States Board of Tax Appeals, and the same is approved by the undersigned as attorney for Great Western Power Company of California.

Approved and ordered filed this 10th day of Jan., 1935.
(S.) Ernest H. Van Fossan, Member.

IN UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

[Title omitted]

PRÆCIPE FOR RECORD

To the Clerk of the United States Board of Tax Appeals:

You will please prepare, transmit and deliver to the Clerk of the United States Circuit Court of Appeals for the Sec-
[fol. 217] ond Circuit, copies duly certified as correct of the following documents and records in the above-entitled cause in connection with the petition for review by the said Circuit Court of Appeals for the Second Circuit, heretofore filed by the Commissioner of Internal Revenue:

1. Docket entries of the proceedings before the Board.
2. Pleadings before the Board:

(a) Petition filed May 2, 1930, including annexed copy of deficiency notice.
(b) Answer filed June 16, 1930.
(c) First Amended Petition, filed September 19, 1933.
(d) Answer to First Amended Petition, filed September 19, 1933.

(e) Commissioner's Notice of Settlement under Rule 50, filed June 6, 1934.

3. Opinions, Decisions and Orders of the Board:

(a) Report promulgated April 26, 1934.
(b) Motion to Amend Opinion, filed June 6, 1934, including "Granted" stamp endorsed thereon.
(c) Decision entered June 26, 1934.

4. Commissioner's Petition for Review and Assignments of Error, captioned in the United States Circuit Court of Appeals for the Second Circuit.

[fol. 218] 5. Court Order dated October 10, 1934, correcting clerical error in Petition for Review, together with copy of Motion to Correct Record.

6. (a) Notice to taxpayer of filing Petition for Review, together with acknowledgment of service.
(b) Notice to counsel of filing Petition for Review, together with acknowledgment of service.

7. Statement of the Evidence as settled and allowed.
8. Orders enlarging time for preparation of the evidence and for transmission and delivery of the record.
9. This Præcipe.

(Signed) Robert H. Jackson, Assistant General Counsel for the Bureau of Internal Revenue.

Service of a copy of the within Præcipe is hereby admitted this 20th day of Dec., 1934.

(Signed) Thomas R. Dempsey, Attorney for Respondent.

[fol. 219] Clerk's certificate to foregoing transcript omitted in printing.

[fol. 220] IN THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

B. T. A. Docket No. 48617

GUY T. HELVERING, Commissioner of Internal Revenue, Petitioner,

v.

GREAT WESTERN POWER COMPANY of California, Respondent

Note of Issue

MOTION TO DISMISS FOR LACK OF JURISDICTION

For the motion: Thomas R. Dempsey; A. Calder Mackay; Hugh Satterlee.

Opposing the motion: Frank J. Wideman, Assistant United States Attorney General; Robert H. Jackson, Assistant General Counsel; Bureau of Internal Revenue; Paul E. Waring, Special Attorney, Bureau of Internal Revenue.

Motion returnable April 8, 1935.

Com. Int. Rev. v. Gt. Western Co. Note of Issue. United States Circuit Court of Appeals, Second Circuit. Filed Mar. 29, 1935. William Parkin, Clerk.

[fol. 221] UNITED STATES CIRCUIT COURT OF APPEALS, SECOND CIRCUIT

At a Stated Term of the United States Circuit Court of Appeals, in and for the Second Circuit, held at the Court Rooms in the Post Office Building in the City of New York, on the 15th day of April, one thousand nine hundred and thirty-five.

Present: Hon. Martin T. Manton, Hon. Learned Hand, Hon. Augustus N. Hand, Circuit Judges.

COMMISSIONER OF INTERNAL REVENUE, Petitioner,

vs.

GREAT WESTERN POWER COMPANY of California, Respondent

A motion having been made herein by counsel for the respondent to dismiss the appeal for lack of jurisdiction;

Upon consideration thereof it is

Ordered that said motion be and hereby is granted so far as it relates to the determination as to the years 1925 and 1926, and denied so far as it relates to the determination as to the year 1924.

Wm. Parkin, Clerk.

[fol. 222] [Endorsed:] United States Circuit Court of Appeals, Second Circuit. Commissioner of Internal Revenue vs. Great Western Power Company of California. Order. United States Circuit Court of Appeals, Second Circuit. Filed Apr. 15, 1935. William Parkin, Clerk.

[fol. 223] IN THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

No. 402

COMMISSIONER OF INTERNAL REVENUE, Petitioner,

v.

GREAT WESTERN POWER COMPANY of California, Respondent

MOTION

Comes now the Respondent, by its counsel of record, and moves this Honorable Court to disregard the brief of the Petitioner under Rule 10 of this Court and to dismiss the above entitled appeal for the following reasons:

1. This case involves an appeal from a decision of the United States Board of Tax Appeals.

2. In his petition for review and assignments of error the only errors assigned by the Petitioner related to the insufficiency of the evidence to support the findings of the said Board.

3. It now appears from the brief filed by the Petitioner that such assignments of error have been abandoned and

that the said brief is not directed to any matter assigned as error in the aforesaid assignments of error.

Thomas R. Dempsey, A. Calder Mackay, Attorneys for Respondent.

[fol. 224] UNITED STATES CIRCUIT COURT OF APPEALS, SECOND CIRCUIT

At a Stated Term of the United States Circuit Court of Appeals, in and for the Second Circuit, held at the Court Rooms in the Post Office Building in the City of New York, on the 28th day of May, one thousand nine hundred and thirty-five.

Present: Hon. Learned Hand, Hon. Augustus N. Hand, Hon. Harrie B. Chase, Circuit Judges.

COMMISSIONER OF INTERNAL REVENUE, Petitioner,

vs.

GREAT WESTERN POWER COMPANY of California, Respondent

A motion having been made herein by counsel for the respondent to dismiss the appeal upon the ground that the assignments of error had been abandoned.

Upon consideration thereof it is

Ordered that said motion be and hereby is denied.

Wm. Parkin, Clerk.

[fol. 225] [Endorsed:] United States Circuit Court of Appeals, Second Circuit. Commissioner of Internal Revenue vs. Great Western Power Company of California. Order. United States Circuit Court of Appeals, Second Circuit. Filed Jun. 3, 1935. William Parkin, Clerk.

[fol. 226] UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

COMMISSIONER OF INTERNAL REVENUE, Petitioner,

against

GREAT WESTERN POWER COMPANY of California, Respondent

Before L. Hand, Augustus N. Hand and Chase, Circuit Judges

Petition to review a decision of the Board of Tax Appeals disallowing a deficiency in the income taxes of the respond-

ent for the year 1924. Originally, deficiencies for the years 1920 and 1926 were in issue but a motion to dismiss as to those years was allowed. Reversed.

Frank J. Wideman, Assistant Attorney General; Sewall Key, and A. F. Prescott, Special Assistants to the Attorney General; Thomas R. Dempsey, A. Calder Mackay, Attorneys for Respondent.

CHASE, Circuit Judge:

During the taxable period the respondent was a public utility corporation of the State of California subject to the jurisdiction of the California State Railroad Commission. [fol. 227] It kept its books on the accrual basis in accordance with the orders of said commission and filed its income tax return on the accrual basis. The Board held that it was entitled to deduct as a loss the entire unamortized discount, expenses of issuance, premiums paid, and expenses of retirement of certain of its bonds retired in 1924 in accordance with the terms under which the bonds had been issued. At that time the holders exercised their option to receive, and did receive, for the called bonds a cash premium of 5% and bonds of the respondent of another series of the same par value. To review this decision the Commissioner filed the instant petition.

During 1921, the respondent issued and sold its General Lien 8% Gold Bonds dated February 1, 1921 and due February 1, 1936 to the face value of $2,500,000.00. These bonds were secured by what is known as its General Lien Indenture dated February 1, 1921 wherein its property was, subject to prior encumbrances, mortgaged and conveyed in trust for the benefit of these bondholders. These bonds were sold at a discount of $150,000.00 and the expense of their issuance was $22,283.54. They were subject to call by the respondent before maturity and, if called, the holders were entitled at their option to receive in exchange for them 105% in cash or a 5% premium in cash and bonds known as Series B 7's of the same par value.

The bonds known as Series B 7's were issued by the respondent in 1921; were dated August 1, 1920; and were due August 1, 1950. This issue was of the par value of $8,500,00-.00. Of these bonds $2,500,000.00 in par value were delivered to the trustees under the General Lien In-

denture and held by such trustees as additional security [fol. 228] for the bonds known as General Lien 8's and so held that they might be available for distribution to such holders of the General Lien 8's as should elect to take them if and when the 8's should be called. Of the remainder of the issue Series B 7's, $1,000,000.00 in par value were sold to the public for cash at a discount of $100,000.00 and the remainder delivered to trustees as additional security for another issue of bonds not here involved.

By December 31, 1923, the respondent had purchased for cash and retired its General Lien 8's of the par value of $11,000.00 and had charged off the proportionate amount of unamortized discount and expense of issuance as a loss in the year of retirement. This left General Lien 8's outstanding to the face value of $2,489,000.00 on May 8, 1924 and on that date the respondent's board of directors passed a resolution for the redemption of the remainder of the issue. On August 1, 1924, holders of these bonds to the face value of $2,354,000.00, having elected to exercise their option to take in exchange Series B 7's plus the 5% premium in cash, were paid a cash premium of $117,725.00 and given Series B 7's par for *par for* their General Lien 8's which were then retired. The unamortized discount applicable to the bonds so converted was $126,176.97 as of August 1, 1924 and the expense of conversion was $1,461.05. The respondent attempted to take as a deduction in 1924 the sum of the three items viz: the premium paid, the unamortized discount and the expense of conversion making in all $245,363.02. The Commissioner, however, deter- [fol. 229] mined that such amount should be amortized over the life of the Series B 7's exchanged for the General Lien 8's and allowed only $2,027.96 to be deducted in 1924. The decision of the Board reversing the Commissioner and allowing the entire deduction claimed is the only point now up for review.

The remainder of the General Lien 8's outstanding as of August 1, 1924 after the conversion above mentioned were then purchased by the respondent for cash and retired. The Commissioner now concedes that the premium paid on those bonds together with the unamortized discount and the expense of retirement applicable to them was an allowable deduction from 1924 income.

So far as was necessary, the $2,500,000.00 in face value of the Series B. 7's which were delivered to the trustees under the General Lien Indenture were used to make the exchange with the holders of $2,354,500.00 in face value of the General Lien 8's. Of the remainder of $145,500.00 in face value of the Series B 7's held by those trustees $11,000.00 in face value were returned to the respondent because of its previous purchase from the public for cash and the retirement of that amount face value of General Lien 8's and the remainder was returned to the respondent because of its redemption for cash after the call date of a like amount par value of the 8's. None of these Series B 7's so returned to the respondent were reissued.

The respondent's income for 1924 was reported in a consolidated return filed in the name of Western Power Corporation, 25 Broad St., New York, N. Y.

It is clear, as the Commissioner has conceded in respect [fol. 230] to the General Lien 8's retired for cash before maturity, that the unamortized discount plus premium paid plus the expense of retirement is an allowable deduction in the year of retirement. Reg. 65; Art. 545 (3). This regulation so provides and has been in force since it was promulgated under the Revenue Act of 1924. In re-enacting the applicable statute since then Congress has indicated its approval of this administrative interpretation of the law. National Lead Company v. United States, 252 U. S. 140; Brewster v. Gage, 280 U. S. 327; McCaughn v. Hershey Chocolate Co. 283 U. S. 488; Murphy Oil Co. v. Burnet, 287 U. S. 299. See, also United States v. Kirby Lumber Co. 284 U. S. 1.

The problem before us is to determine whether a like complete deduction is allowable in the same year when the retirement is not wholly for cash but is to the extent of the par value an exchange of bonds for bonds in accordance with the terms under which the retired bonds were issued. This precise question has been decided in favor of the respondent in San Joaquin Light & Power Corp. v. McLaughlin, 65 Fed. (2) 677 (C. C. A. 9). It is also said that Commissioner v. Coastwise Transportation Company, 62 Fed. (2) 332 (C. C. A. 1), see also 71 Fed. (2) 104, is to the same effect but in that case the exchange held to result in taxable income was not made pursuant to the contract under which the retired notes were issued but on the contrary merely in

accordance with the voluntary agreement of the parties at the time of retirement to exchange those notes for a lesser amount in face value of bonds. The acceptance of bonds for notes, under any conditions, was no part of the original [fol. 231] note contracts. Moreover, the exchange did reduce the outstanding indebtedness of the taxpayer to the amount of the difference between the face value of the notes and that of the bonds substituted for them. Whatever uncertainty there was as to whether the substituted bonds were the actual equivalent of a payment in cash was immaterial since the transaction made it impossible for the retirement of the notes ever to cost the taxpayer more than the face of the bonds exchanged for them and so to the extent of the difference between the face value of the notes and that of the bonds the taxpayer received at least as much benefit as it could have received if it had paid the face value of the bonds in cash to retire the notes. Had it paid such cash for them the difference would have been taxable income. Kirby v. United States, supra.

By calling the General Lien 8's before maturity this taxpayer made available to the holders of the General Lien 8's the option contained in the terms of these bonds to compel the taxpayer to issue to them Series B 7's as part of the price of redemption. Those who did so require Series B 7's to be delivered to them were merely satisfied pro tanto by the receipt of different obligations of the taxpayer. The taxpayer by so doing received in fact for its Series B 7's thus placed in the hands of the public the net amount it had received for the 8's so retired less the expense of issuing those Series B 7's and the additional cost of retiring the 8's so exchanged. The difference between the face value of the 7's and the amount received for them represents the unamortized discount upon those bonds.

[fol. 232] It will become a realized loss when the bonds are paid at par and, of course, there will be some loss when, if ever, the bonds are retired for less than par but for more than what the taxpayer received for them. The decisive point now is that in 1924 the General Lien 8's were not paid so as to establish a deductible loss. The taxpayer substituted one form of obligation for another leaving the debt to the extent of the face value of the substituted bonds still a debt. Only the evidence of that debt was changed. The amount which will eventually have to be paid to discharge

the debt was not determined in 1924 nor will it be until some future time. Then only will a deductible loss, or perhaps a taxable profit, be realized. Then, if there is a loss, it will be realized from the standpoint of taxation. Losses must be realized to be deductible just as income must be realized to be taxable. Weiss v. Wiener, 279 U. S. 333.

But the annual cost of the use of money which the taxpayer has really received for its Series B 7's is represented not only by the interest it pays on the bonds but the discount, premium and expense of issuance. Helvering v. Union Pacific Co., 293 U. S. 282. In so far as discount is concerned there is a direct provision for its amortization over the life of the bonds. T. R. 45; Art. 545 (3) (a). It is thus "realized" from year to year. While there is no such direct authority for the pro rata deduction of premium and issuance expense it may be accrued and when a taxpayer properly makes a return on the accrual basis, as this taxpayer did, such expense may also be amortized over the life [fol. 233] of the bonds and proportionate annual deductions allowed. Helvering v. Union Pacific Co., supra. This annual deductible expense has been recognized by the Commissioner for the year in question. What is claimed by the taxpayer as a deductible loss for that year must for the reasons stated await deduction when, if ever, any part of it becomes a realized loss. Otherwise it will be deductible only in pro rata annual installments as part of the expenses of the business.

Decision reversed and deduction disallowed.

[fol. 233½] [Endorsed:] United States Circuit Court of Appeals, Second Circuit. Com'r Internal Revenue v. Great Western Power Co. (Copy) Opinion. Chase, Circuit Judge.

[fol. 234] UNITED STATES CIRCUIT COURT OF APPEALS, SECOND CIRCUIT

At a Stated Term of the United States Circuit Court of Appeals, in and for the Second Circuit, held at the Court Rooms in the Post Office Building in the City of New York, on the 29th day of July one thousand nine hundred and thirty-five.

Present: Hon. Learned Hand, Hon. Augustus N. Hand, Hon. Harrie B. Chase, Circuit Judges.

228

COMMISSIONER OF INTERNAL REVENUE, Petitioner,

vs.

GREAT WESTERN POWER COMPANY of California, Respondent

Appeal from the United States Board of Tax Appeals

This cause came on to be heard on the transcript of record from the United States Board of Tax Appeals, and was argued by counsel.

On consideration whereof, it is now hereby ordered, adjudged, and decreed that the order of said United States Board of Tax Appeals be and it hereby is reversed with instructions to disallow the deduction.

It is further ordered that a Mandate issue to the said Board in accordance with this decree.

Wm. Parkin, Clerk.

[fol. 235] [Endorsed:] United States Circuit Court of Appeals, Second Circuit. Commissioner of Internal Revenue vs. Great Western Power Company of California. Order for Mandate. United States Circuit Court of Appeals, Second Circuit. Filed Aug. 1, 1935. William Parkin, Clerk.

[fol. 236] UNITED STATES OF AMERICA,
Southern District of New York:

I, William Parkin, Clerk of the United States Circuit Court of Appeals for the Second Circuit, do hereby certify that the foregoing pages, numbered from 1 to 235, inclusive, contain a true and complete transcript of the record and proceedings had in said Court, in the case of Commissioner of Internal Revenue, Petitioner, against Great Western Power Company of California, Respondent, as the same remain of record and on file in my office.

In testimony whereof, I have caused the seal of the said Court to be hereunto affixed, at the City of New York, in the Southern District of New York, in the Second Circuit, this 25th day of September, in the year of our Lord one thousand nine hundred and thirty-five, and of the Independence of the said United States the one hundred and sixtieth.

Wm. Parkin, Clerk. (Seal United States Circuit Court of Appeals, Second Circuit.)

BLANK

PAGE

[fol. 237] SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed November 18, 1935

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

Endorsed on cover: File No. 40,079. U. S. Circuit Court of Appeals, Second Circuit. Term No. 525. Great Western Power Company of California, petitioner, vs. Commissioner of Internal Revenue. Petition for a writ of certiorari and exhibit thereto. Filed October 17, 1935. Term No. 525, O. T. 1935.

(7275-C)

FILE COPY

FILED
OCT 17 1
CHARLES ELMORE

IN THE

SUPREME COURT

OF THE

UNITED STATES.

OCTOBER TERM, 1935.

No. 525

Great Western Power Company of California,

Petitioner,

vs.

Commissioner of Internal Revenue,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS, SECOND CIRCUIT, AND BRIEF IN SUPPORT THEREOF.

THOMAS R. DEMPSEY,
A. CALDER MACKAY,
1104 Pacific Mutual Building,
Los Angeles, California,
Attorneys for Petitioner.

Parker, Stone & Baird Co., Law Printers, Los Angeles.

TOPICAL INDEX.

PAGE

Petition for Writ of Certiorari to the United States Circuit Court of Appeals, Second Circuit 3

A.

Summary Statement of the Matter Involved 4

I.

History of the Case 4

II.

Question Involved 5

Is the petitioner, in the determination of its net taxable income for the year 1924, entitled to take as a deduction on account of the retirement of its bonds the unamortized discount and expenses of issuing said bonds and expenses and premiums paid in the retirement thereof? 5

III.

Statement of Facts 5

B.

Reasons for Granting the Petition 8

Brief in Support of Petition for Writ of Certiorari to the United States Circuit Court of Appeals, Second Circuit 11

I.

Opinions Below 11

II.

Jurisdiction 12

PAGE

III.

Question Involved 13

Is the petitioner in the determination of its net taxable income for the year 1924 entitled to take as a deduction on account of the retirement of its bonds the unamortized discount and expenses of issuing said bonds and expenses and premiums paid in the retirement thereof? 13

IV.

Assignments of Error 13

V.

Statutes and Regulations Involved 14

VI.

Law and Argument 14

TABLE OF AUTHORITIES CITED.

CASES.

PAGE

American Chicle Co., 23 B. T. A. 291 20

Brewster v. Gage, 280 U. S. 327 16

Commissioner v. Coastwise Transportation Corp., 62 F. (2d) 332; 71 F. (2d) 104 8

Commissioner of Internal Revenue v. Coastwise Transportation Company, 62 F. (2d) 332 17

Detroit Garages Inc., B. T. A. memorandum opinion unreported, July 13, 1934 20

East Ninth Euclid Co., 26 B. T. A. 32 20

Fawcus Machine Co. v. United States, 282 U. S. 375 16

Helvering v. California Oregon Power Co., C. A. of D. C., 75 F. (2d) 644 ..... 16, 20

Helvering v. Central States Electric Corp., 76 F. (2d) 1011 20

Helvering v. Union Public Service Co., 75 F. (2d) 723 20

McCaughn v. Hershey Chocolate Co., 283 U. S. 488 16

Murphy Oil Co. v. Burnet, 287 U. S. 299 16

National Lead Company v. United States, 252 U. S. 140 16

Old Colony Trust Company, et al., Executors, v. Commissioner, 279 U. S. 716, Sec. 240, Judicial Code, 28 U. S. C. A. 347 12

San Joaquin Light & Power Corporation v. John P. McLaughlin, Collector of Internal Revenue, 65 F. (2d) 677 ..... 4, 8, 13, 14, 17, 20

United States v. Kirby Lumber Co., 284 U. S. 1 ..... 8, 14, 15, 17, 19, 20, 21, 22

United States Board of Tax Appeals, 30 B. T. A. 503 11

Universal Battery Co. v. United States, 281 U. S. 580 16

STATUTES.

Act of Congress, approved February 26, 1926, Sec. 274(a) "Revenue Act of 1926" (44 Stat. 55; 26 U. S. C. A. Sec. 1048 12

PAGE

Act of Congress, approved February 26, 1926, Secs. 1001, 1002 and 1003, "Revenue Act of 1926" (44 Stat. 1, 109, 110, 26 U. S. C. A., Secs. 1224, 1225, 1226 12

Act of Congress, approved May 29, 1928, Sec. 603, "Revenue Act of 1928" (45 Stat. 873, 26 U. S. C. A., Sec. 1224 12

Act of Congress approved June 6, 1932, Sec. 1101, "Revenue Act of 1932" (47 Stat. 286), amended by section 519 of the Act of Congress, approved May 10, 1934, "Revenue Act of 1934" (48 Stat. 760, 26 U. S. C. A., Sec. 1225 12

REGULATIONS.

Internal Revenue Regulations 65, Art. 545 8

Regulations 45, Revenue Act of 1918, Art. 544 16

Regulations 62, Art. 545 17

Regulations 62, Revenue Act of 1921, Art. 545 16

Regulations 65, Art. 545 16

Regulations 65, Revenue Act of 1924, Art. 545, Subd. (3) 15

Regulations 69, Art. 545 17

Regulations 69, 1926 Act, Art. 545 16

Regulations 74, 1928 Act, Art. 68 16

Regulations 77, 1932 Act, Art. 68 16

Regulations 86, 1934 Act, Art. 22(a) (18) 16

Regulations 86, February 11, 1935, Art. 22(a) (18) 17

INDEX TO APPENDIX.

PAGE

Revenue Act of 1924, c. 234, 43 Stat. 253, Sec. 234 (a) 25

Revenue Act of 1926, Sec. 1002 25

Revenue Act of 1934, c. 277, 48 Stat. 680, Sec. 519 25

Treasury Regulations 65, promulgated under the Revenue Act of 1924, Art. 545 26

Treasury Regulations 65, promulgated under the Revenue Act of 1924, Art. 563 26

IN THE

SUPREME COURT

OF THE

UNITED STATES.

OCTOBER TERM, 1935.

No.....

Great Western Power Company of California,

Petitioner,

vs.

Commissioner of Internal Revenue,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS, SECOND CIRCUIT.

To the Honorable Chief Justice and Associate Justices of the Supreme Court of the United States:

Petitioner, Great Western Power Company of California, respectfully shows to this Honorable Court that this is a petition for writ of certiorari to the Circuit Court of Appeals for the Second Circuit to review a decision made and entered by that court on July 22, 1935, reversing the decision of the United States Board of Tax Appeals.

A.

SUMMARY STATEMENT OF THE MATTER INVOLVED.

I.

HISTORY OF THE CASE.

This controversy was originated by a deficiency letter issued by the Commissioner of Internal Revenue on March 4, 1930, proposing additional taxes against the petitioner for the year 1924 of $26,293.40.

A timely appeal was taken by petitioner to the United States Board of Tax Appeals in which there was presented the question of whether petitioner, in determining its net taxable income for the year 1924, was entitled to take as a deduction its unamortized discount and expenses of issuing bonds and expenses and premiums paid on the retirement of bonds during said year. The Board of Tax Appeals held in favor of the petitioner, basing its opinion upon the decision of the United States Circuit Court of Appeals for the Ninth Circuit in the case of *San Joaquin Light & Power Corporation v. John P. McLaughlin, Collector of Internal Revenue,* 65 F. (2d) 677. The United States Circuit Court of Appeals for the Second Circuit reversed the Board of Tax Appeals and disallowed the deductions. The final decision of the Circuit Court of Appeals for the Second Circuit was entered on July 22, 1935. [R. p. .....]

II.

QUESTION INVOLVED.

Is the Petitioner, in the Determination of Its Net Taxable Income for the Year 1924, Entitled to Take as a Deduction on Account of the Retirement of Its Bonds the Unamortized Discount and Expenses of Issuing Said Bonds and Expenses and Premiums Paid in the Retirement Thereof?

III.

STATEMENT OF FACTS.

During the year 1924 the Great Western Power Company of California, petitioner herein, was a public utility corporation and as such was subject to the jurisdiction of the California State Railroad Commission and kept its books on the accrual basis in accordance with the classification of accounts prescribed by the said commission. [R. p. 110.] During the year 1921 the petitioner issued and sold its General Lien 8% Gold Bonds dated February 1, 1921, and due February 1, 1936 to the face value of $2,500,000.00. These bonds were secured by what is known as its General Lien Indenture dated February 1, 1921, wherein its property was, subject to prior encumbrances, mortgaged and conveyed in trust for the benefit of these bondholders. These bonds were sold at a discount of $150,000.00 and the expense of their issuance was $22,283.54. [R. p. 112.] They were subject to call by the petitioner before maturity and, if called, the holders were entitled at their option to receive in exchange for them 105% in cash or a 5% premium in cash and bonds known as Series B 7's of the same par value. [R. p. 167.]

The bonds known as Series B 7's were dated August 1, 1920, and were issued by the petitioner in 1921. They were due August 1, 1950. This issue was of the par value of $8,500,000.00. [R. p. 114.] Of these bonds $2,500,000.00 in par value were delivered to the trustees under the General Lien Indenture and held by such trustees as additional security for the bonds known as General Lien 8's and so held that they might be available for distribution to such holders of the General Lien 8's as should elect to take them if and when the 8's should be called. Of the remainder of the issue Series B 7's, $1,000,000.00 in par value were sold to the public for cash at a discount of $100,000.00 and the remainder delivered to trustees as additional security for another issue of bonds not here involved. [R. p. 114.]

By December 31, 1923, the petitioner had purchased for cash and retired its General Lien 8's of the par value of $11,000.00 and had charged off the proportionate amount of unamortized discount and expense of issuance as a loss in the year of retirement. [R. p. 112.] This left General Lien 8's outstanding to the face value of $2,489,000.00 on May 8, 1924, and on that date petitioner's board of directors passed a resolution for the redemption of the remainder of the issue. On August 1, 1924, holders of these bonds to the face value of $2,354,000.00, having elected to exercise their option to take in exchange Series B 7's plus the 5% premium in cash, were paid a cash premium of $117,725.00 and given Series B 7's par for par for their General Lien 8's which were then retired. [R. pp. 112-113.] The unamortized discount applicable to the bonds so converted was $126,176.97 as of August 1, 1924, and the expense of

conversion was $1,461.05. The petitioner attempted to take as a deduction in 1924 the sum of these three items, namely, the premium paid, the unamortized discount and the expense of conversion, making in all $245,363.02. The Commissioner of Internal Revenue, however, determined that such amount should be amortized over the life of the Series B 7's exchanged for the General Lien 8's and allowed only $2,027.96 to be deducted in 1924. [R. p. 113.]

The remainder of the General Lien 8's outstanding as of August 1, 1924 after the conversion above mentioned were then purchased by the petitioner for cash and retired. The commissioner concedes that the premium paid on these bonds, together with the unamortized discount and the expense of retirement applicable to them, was an allowable deduction from 1924 income. [R. p. 113.]

So far as was necessary, the $2,500,000.00 in face value of the Series B 7's which were delivered to the trustees under the General Lien Indenture were used to make the exchange with the holders of $2,354,500.00 in face value of the General Lien 8's. Of the remainder of $145,500.00 in face value of the Series B 7's held by those trustees $11,000.00 in face value were returned to the petitioner because of its previous purchase from the public for cash and the retirement of that amount face value of General Lien 8's and the remainder was returned to the petitioner because of its redemption for cash after the call date of a like amount par value of the 8's. None of these Series B 7's so returned to the petitioner were reissued. [R. p. 115.]

The United States Board of Tax Appeals decided in favor of petitioner and held that the deductions were

allowable, the decision of the Board being based upon the decision of the United States Circuit Court of Appeals for the Ninth Circuit in the case of *San Joaquin Light & Power Corporation v. John P. McLaughlin, Collector of Internal Revenue,* 65 F. (2d) 677. In the instant case the Circuit Court of Appeals for the Second Circuit reversed the Board and held that the deductions were not allowable.

B.

REASONS FOR GRANTING THE PETITION.

1. The decision of the United States Circuit Court of Appeals for the Second Circuit is in direct conflict with the decision of the United States Circuit Court of Appeals for the Ninth Circuit rendered in the case of *San Joaquin Light & Power Corporation v. John P. McLaughlin, Collector of Internal Revenue,* 65 F. (2d) 677.

2. The decision of the United States Circuit Court of Appeals for the Second Circuit is in conflict with the decision of this Honorable Court in the case of *United States v. Kirby Lumber Co.,* 284 U. S. 1.

3. The decision of the United States Circuit Court of Appeals for the Second Circuit is in conflict with the decision of the United States Circuit Court of Appeals for the First Circuit rendered in the case of *Commissioner v. Coastwise Transportation Corp.,* 62 F. (2d) 332 (see also 71 F. (2d) 104).

4. The decision of the United States Circuit Court of Appeals for the Second Circuit is in conflict with the provisions of Article 545 of Regulations 65 promulgated by the Commissioner of Internal Revenue with the approval of the Secretary of the Treasury, which regulations have

been in force and effect for many years, during which time there have been repeated re-enactments of the statute.

5. The issues in this case also present important questions of federal law which have not been but should be settled by this Honorable Court.

Wherefore, your petitioner respectfully prays that a writ of certiorari be issued out of and under the seal of this Honorable Court, directed to the United States Circuit Court of Appeals for the Second Circuit, commanding the court to certify and send to this Court for its review and determination, on a day certain to be therein named, a full and complete transcript of the record of all proceedings in the case numbered and entitled Docket No. 402, *Commissioner of Internal Revenue, Petitioner, v. Great Western Power Company of California, Respondent,* and that the judgment of the Circuit Court of Appeals for the Second Circuit may be reversed by this Honorable Court, and that your petitioner may have such other and further relief in the premises as to this Honorable Court may seem meet and just; and your petitioner will ever pray.

Respectfully submitted,

THOMAS R. DEMPSEY,
A. CALDER MACKAY,
Attorneys for Petitioner.

1104 Pacific Mutual Building,
Los Angeles, California.

IN THE

SUPREME COURT

OF THE

UNITED STATES.

OCTOBER TERM, 1935.

No.....

Great Western Power Company of California,

Petitioner,

vs.

Commissioner of Internal Revenue,

Respondent.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS, SECOND CIRCUIT.

I.

Opinions Below.

The opinion of the United States Circuit Court of Appeals for the Second Circuit was rendered, entered and filed on July 22, 1935, unreported to date. [R. pp. .....] The opinion of the United States Board of Tax Appeals was promulgated on April 26, 1934 [R. pp. 61-77], 30 B. T. A. 503.

II.

Jurisdiction.

1. The judgment to be reviewed was entered on July 22, 1935. The time to apply for a writ of certiorari, therefore, runs from this date.

2. The Board of Tax Appeals had jurisdiction of this case under section 274 (a) of the Act of Congress, approved February 26, 1926, entitled the "Revenue Act of 1926" (44 Stat. 55; 26 U. S. C. A., Sec. 1048). The appeal to the Circuit Court of Appeals was taken in pursuance of the provisions of sections 1001, 1002 and 1003 of the Act of Congress, approved February 26, 1926, entitled the "Revenue Act of 1926" (44 Stat. 1, 109, 110, 26 U. S. C. A., Sections 1224, 1225, 1226), as amended by section 603 of the Act of Congress, approved May 29, 1928, entitled the "Revenue Act of 1928" (45 Stat. 873, 26 U. S. C. A., Section 1224), as amended by section 1101 of the Act of Congress approved June 6, 1932, entitled the "Revenue Act of 1932" (47 Stat. 286), and as further amended by section 519 of the Act of Congress, approved May 10, 1934, entitled the "Revenue Act of 1934" (48 Stat. 760, 26 U. S. C. A., Section 1225).

3. This court has jurisdiction to review the judgment of the Circuit Court of Appeals. *Old Colony Trust Company, et al., Executors, v. Commissioner,* 279 U. S. 716, section 240, *Judicial Code,* 28 U. S. C. A. 347.

III.

Question Involved.

IS THE PETITIONER IN THE DETERMINATION OF ITS NET TAXABLE INCOME FOR THE YEAR 1924 ENTITLED TO TAKE AS A DEDUCTION ON ACCOUNT OF THE RETIREMENT OF ITS BONDS THE UNAMORTIZED DISCOUNT AND EXPENSES OF ISSUING SAID BONDS AND EXPENSES AND PREMIUMS PAID IN THE RETIREMENT THEREOF?

IV.

Assignments of Error.

(1) The United States Circuit Court of Appeals for the Second Circuit erred in reversing the board and in holding that the sum of $245,363.02 representing premiums, unamortized discount and expenses paid by petitioner in the retirement of $2,354,500.00 face amount of its General Lien 8% bonds was not deductible in the determination of petitioner's net taxable income for the year 1924.

(2) The United States Circuit Court of Appeals for the Second Circuit erred in reversing the decision of the United States Board of Tax Appeals.

(3) The United States Circuit Court of Appeals for the Second Circuit erred in failing to follow the decision of the United States Circuit Court of Appeals for the Ninth Circuit in the case of *San Joaquin Light & Power Corporation v. John P. McLaughlin, Collector of Internal Revenue*, 65 F. (2d) 677.

V.

Statutes and Regulations Involved:

See Appendix pages 25-26.

VI.

Law and Argument.

The Revenue Act of 1924 provides that a taxpayer may take as a deduction in the determination of its net taxable income, among other things, losses sustained and interest paid during the taxable year. The regulations of the Commissioner of Internal Revenue promulgated with the approval of the Secretary of the Treasury, have consistently provided that in the retirement of bonds a taxpayer is entitled to take as a deduction during the year of retirement its unamortized bond discount and expense of issuing as well as the premiums and expenses paid in the retirement thereof.

The regulations also provide that where bonds are redeemed for less than their issuing price the corporation sustains a taxable gain. This Honorable Court in the case of *United States v. Kirby Lumber Company,* 284 U. S. 1, approved these regulations and held that a corporation purchasing or redeeming its bonds below the issuing price realized a taxable gain. The case at bar involves the converse of the foregoing proposition, namely, that a taxpayer suffers a deductible loss in the retirement of its bonds at a price in excess of the issuing price.

The Ninth Circuit Court of Appeals in the case of *San Joaquin Light & Power Corporation v. John P. McLaughlin,* 65 F. (2d) 677, held that a corporation did suffer a de-

ductible loss in the retirement of its bonds at a price in excess of the issuing price. This court, last named, held that when bonds are retired the unamortized bond discount and expense of issuing the bonds as well as the premiums and expenses paid in the retirement thereof were deductible. The decision of the Ninth Circuit Court of Appeals in the above mentioned case is directly in conflict with the decision of the Second Circuit Court of Appeals in the case at bar. It is further respectfully submitted that the decision of the Second Circuit Court of Appeals is directly in conflict with the decision of this Honorable Court in the case of *United States v. Kirby Lumber Company,* 284 U. S. 1.

As heretofore stated, the regulations promulgated by the Commissioner of Internal Revenue with the approval of the Secretary of the Treasury have consistently permitted the deduction claimed by petitioner.

Subdivision (3) of Article 545 of Regulations 65 promulgated under the Revenue Act of 1924 provides in part as follows:

> "(a) If bonds are issued by a corporation at a discount, the net amount of such discount is deductible and should be prorated or amortized over the life of the bonds. (b) If thereafter the corporation purchases and retires any of such bonds at a price in excess of the issuing price plus any amount of discount already deducted, the excess of the purchase price over the issuing price plus any amount of discount already deducted (or over the face value minus any amount of discount not yet deducted) is a deductible expense for the taxable year."

This Article applies specifically to all phases of bond discount, and it has been held likewise to apply to the expense of issuing bonds. (*Helvering v. California Oregon Power Co.*, C. A. of D. C., decided January 7, 1935; 75 F. (2d) 644).

Article 545 of Regulations 65 is the same as Article 545 of Regulations 62 promulgated under the Revenue Act of 1921, and the same as Article 544 of Regulations 45 promulgated under the Revenue Act of 1918. It has been continued without change under each of the Revenue Acts since 1924. See Article 545 of Regulations 69 (1926 Act), Article 68 of Regulations 74 (1928 Act), Article 68 of Regulations 77 (1932 Act), and Article 22 (a) (18) of Regulations 86 (1934 Act).

Since this article of the regulations was first promulgated in its present form Congress has six times reenacted the statute upon which it is based. The repeated re-enactment of the statute in the face of consistent administrative construction amounts to legislative approval of the statute as so construed. (*National Lead Company v. United States*, 252 U. S. 140; *Brewster v. Gage*, 280 U. S. 327; *Universal Battery Co. v. United States*, 281 U. S. 580; *Fawcus Machine Co. v. United States*, 282 U. S. 375; *McCaughn v. Hershey Chocolate Co.*, 283 U. S. 488; *Murphy Oil Co. v. Burnet*, 287 U. S. 299.)

Furthermore, Article 545 of Regulations 62 (which is identical with Article 545 of Regulations 65) has been

expressly approved by this Honorable Court in *United States v. Kirby Lumber Company,* 284 U. S. 1, and by the Circuit Court of Appeals for the Ninth Circuit in *San Joaquin Light and Power Corporation v. McLaughlin,* 65 F. (2d) 677.

We may safely say, therefore, that Article 545 of Regulation 65 is unquestionably a correct exposition of the law.

We would also call to the attention of this Honorable Court the fact that in the cases of *Commissioner of Internal Revenue v. Coastwise Transportation Company,* 62 F. (2d) 332, decided on December 17, 1932, and *San Joaquin Light and Power Corporation v. McLaughlin,* 65 F. (2d) 677, decided on June 19, 1933, the same construction of Article 545 as is now advocated by the respondent herein was refused by the Circuit Court of Appeals for the First and Ninth Circuits, respectively. Since the time of those decisions the Revenue Act of 1934 has been passed in which is embodied the same provisions as contained in the Acts under which those cases were decided, and Article 22 (a) (18) of Regulations 86 promulgated on February 11, 1935, is identical with Article 545 of Regulations 69 and 545 of Regulations 62 considered by the courts in making the above decisions. If the interpretation placed upon those articles by the courts in the above cited cases was erroneous, as the respondent would have us believe that they were (although a writ of *certiorari* was not sought in either case), then it is apparent that in promulgating Regulations 86 the erroneous

interpretation could have been corrected by the simple expedient of wording Article 22 (a) (18) so as to except from its provisions those cases in which new bonds were exchanged for old on the retirement of the latter. The fact that no change was made in the law following these decisions and that no such exception appears in Regulations 86 is, we submit, conclusive evidence that Article 545 as interpreted by the courts in the above cited cases is a correct exposition of the law.

Petitioner during the year 1924 in the retirement of its General Lien 8's paid a cash premium of $117,725.00; its unamortized discount applicable to these bonds amounted to $126,176.97 and the expense of conversion amounted to $1,461.05.

The Circuit Court of Appeals for the Second Circuit in effect held that the cash premium as well as the unamortized bond discount and expense of conversion attached to the Series B 7's which were used by petitioner in the retirement of the General Lien 8's and should, therefore, be spread over the life of the new Series B 7's. Whether the unamortized discount and expense and premium paid on the retirement of the old bonds constitute part of the use of the old money or part of the use of the new money, acquired upon the issuance of the new bonds, is a question of fact and can be answered only by examining the facts. The facts, we respectfully submit, demonstrate conclusively that the unamortized bond discount and expense of issuing and also the premiums and

expenses paid in the retirement of the bonds constituted part of the use of the old money and did not in any wise represent a part of the cost of the new bonds.

In the case of *United States v. Kirby Lumber Co.*, 284 U. S. 1, this Honorable Court held that a corporation purchasing or redeeming its bonds below the issuing price realized a taxable gain. The gain would be realized whether the bonds were retired for cash or property. The mere fact that new bonds were issued as a part consideration for the retirement can have no material bearing. Indeed, it is believed that the respondent will not challenge this statement.

We respectfully submit that the converse of this is true; that where a corporation retires its bonds for an amount in excess of the price of issuance it sustains a deductible loss. Since the Revenue Act recognizes gains and losses from sales and exchanges of property, it does not make any difference whether the bonds were retired for cash or partly for cash and other bonds.

It is respectfully submitted that the petitioner's contention as to the interpretation of Article 545 as applied to the instant case is correct from the standpoint of reason as well as upon the authorities above cited. In view of the recent decisions applying the corresponding articles in the Commissioner's other regulations there can be no doubt but what, if the General Lien 8's here in question had been retired for cash, the petitioner would have been entitled to the deduction claimed, (*United States v.*

Kirby Lumber Co., 284 U. S. 1; *Detroit Garages Inc.*, B. T. A. memorandum opinion unreported, July 13, 1934; *American Chicle Co.*, 23 B. T. A. 291). Nor can there be any doubt but what the same would hold true if the bonds had been retired for cash secured by the issuance and sale of new bonds for the express purpose of making such retirement. (*Helvering v. Union Public Service Co.*, C. C. A. 8, January 2, 1935, 75 F. (2d) 723; *Helvering v. The California Oregon Power Co.*, C. A. of D. C., January 7, 1935, 75 F. (2d) 644; *Helvering v. Central States Electric Corp.*, C. C. A. 2, April 1, 1935, 76 F. (2d) 1011; *San Joaquin Light and Power Co.*, 65 F. (2d) 677; *East Ninth Euclid Co.*, 26 B. T. A. 32.)

The only ground upon which the respondent attempts to distinguish the transaction in the instant case from those involved in the cases next above cited, and thereby remove it from the provisions of Article 545, is that the General Lien 8's here in question were not "purchased and retired" within the meaning of the article. We submit that such a ground for distinction is nonexistent. The holders of the $2,354,500.00 General Lien 8's who participated in the exchange accepted the like amount of Series B 7's and the $117,725.00 in cash as full payment of the petitioner's debt to them under the General Lien Indenture. By such acceptance and the subsequent retirement of these bonds the petitioner's obligation under this indenture was completely extinguished, and thereafter the rights of the persons who accepted the Series B 7's were maintainable solely under the entirely different First and Refunding Mortgage. Petitioner submits that the exchange, therefore, was a purchase and retirement falling squarely within the provisions of Article

545, and that it *required* the deduction in the year 1924 of the then unamortized discount and expense and the premiums paid upon the bonds so retired.

Respondent concedes that the petitioner is entitled to take as a deduction for the year 1924 the same items applicable to the bonds which were retired for cash, but contends that it is otherwise with respect to the bonds retired by the exchange. We are at a loss to understand why any such distinction should be drawn. As pointed out above, if the Series B 7's had been sold on the open market and the proceeds thereof used to retire the General Lien 8's petitioner would unquestionably have been entitled to the deduction. Why is this true? The answer to this question seems to be that as a result of such sale a new liability would have been created to which new incidents would have been attached. This, however, is equally true in the case as it stands. No obligation under the Series B 7's here in question arose until after they had been issued to the holders of the General Lien 8's in exchange for their bonds, and the incidents of this new liability were no different in the hands of these holders than they would have been in the hands of other holders.

Moreover, the General Lien 8's which were redeemed for cash were identically the same as those which were exchanged for the Series B 7's. They were all issued under the same indenture, the rights of all the holders thereof were the same, and they were all retired pursuant to the same call. The indenture was a mortgage on petitioner's property and the retirement of the bonds thereunder released certain of its assets—a deciding factor in determining whether gain or loss is to be recognized on the transaction (*United States v. Kirby Lumber*

Co., 284 U. S. 1), but the bonds which were retired for cash were no more effective in bringing about this release than were the bonds retired by the exchange.

The respondent's contention that the bonds retired by the exchange must be accorded a different treatment than those retired for cash is tantamount to saying that the petitioner's deductions for income tax purposes are dependent upon pure circumstances arising from the voluntary acts of third persons. This is clearly not within the contemplation of any literal construction of the statute and petitioner submits that there is much more merit in the theory adopted by the Board of Tax Appeals in deciding the case below: namely, that the question should be decided on principle and not upon circumstance. We recognize, of course, that a strict construction of a statute sometimes leads to absurd results, and that in such cases it will not be adopted by the courts, but we do not believe that there is any liklihood of such a result from a strict construction of the regulation here in question. On the contrary, we believe that it is only by means of a strict construction that an extremely chaotic condition in the administration of the law can be averted. If the construction advocated by the respondent were to be adopted it would permit the pyramiding of deductions; i. e., it would, in all cases such as this, permit the carrying forward from one bond issue to the next all of the unamortized discount and expense applicable to, and the premiums paid on the retirement of, prior issues. Undoubtedly there are outstanding in this country at the

present time many bond issues which are the outgrowth of prior issues, and it is conceivable that in such cases it would be necessary to go back perhaps fifty years or more to determine the present annual amortization properly applicable to any single issue now outstanding; and it is likewise conceivable that as the result of such pyramiding the present annual amortization charges would be so large as to entirely eliminate the issuing company's annual income. It is respectfully submitted that any such construction of the statute which would not only permit such a result, but would in fact compel it, is clearly unreasonable.

Again we wish to emphasize that the United States Circuit Court of Appeals for the Ninth Circuit in the case of *San Joaquin Light & Power Corporation v. John P. McLaughlin, Collector of Internal Revenue,* 65 F. (2d) 677, had before it the identical issues presented in this matter and that it decided against the contention of the government.

In conclusion, it is respectfully submitted that the policy of the law with respect to the deductions here in question has long since been definitely settled and that nothing is now to be gained by delving into abstract theories in an effort to devise some idealistic method by which such deductions *might* be taken. The regulations provide that they shall be taken when the bonds are purchased and retired; this regulation is reasonable, it is simple of application, it has on numerous occasions been approved by the courts, and now to import to it the theoretical limita-

tion advocated by the respondent can only serve to unsettle the law and make for confusion in its administration.

Wherefore, in view of the foregoing it is urged that this petition be granted in order that this Honorable Court may pass upon this important question, reverse the decision of the United States Circuit Court of Appeals and relieve petitioner of the grievous injustice that has been done it on account hereof.

Respectfully submitted,

THOMAS R. DEMPSEY,
A. CALDER MACKAY,
Attorneys for Petitioner.
1104 Pacific Mutual Building,
Los Angeles, California.

APPENDIX.

Revenue Act of 1924, c. 234, 43 Stat. 253:

SEC. 234. (a) In computing the net income of a corporation subject to the tax imposed by section 230 there shall be allowed as deductions:

(1) All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, * * *.

* * * * * * * * *

(2) All interest paid or accrued within the taxable year on its indebtedness, * * *

Revenue Act of 1934, c. 277, 48 Stat. 680:

SEC. 519. VENUE FOR APPEALS FROM BOARD OF TAX APPEALS.

(a) Section 1002 of the Revenue Act of 1926 is amended to read as follows:

"VENUE

"Sec. 1002. (a) Except as provided in subdivision (b), such decision may be reviewed by the Circuit Court of Appeals for the circuit in which is located the collector's office to which was made the return of the tax in respect of which the liability arises or, if no return was made, then by the Court of Appeals of the District of Columbia.

"(b) Notwithstanding the provisions of subsection (a), such decision may be reviewed by any Circuit Court of Appeals, or the Court of Appeals of the District of Columbia, which may be designated by the Commissioner and the taxpayer by stipulation in writing."

Treasury Regulations 65, promulgated under the Revenue Act of 1924:

ART. 545. *Sale and retirement of corporate bonds.*—

* * * * * * * * *

(3) (a) If bonds are issued by a corporation at a discount, the net amount of such discount is deductible and should be prorated or amortized over the life of the bonds. (b) If thereafter the corporation purchases and retires any of such bonds at a price in excess of the issuing price plus any amount of discount already deducted, the excess of the purchase price over the issuing price plus any amount of discount already deducted (or over the face value minus any amount of discount not yet deducted) is a deductible expense for the taxable year. (c) If, however, the corporation purchases and retires any of such bonds at a price less than the issuing price plus any amount of discount already deducted, the excess of the issuing price plus any amount of discount already deducted (or the face value minus any amount of discount not yet deducted) over the purchase price is gain or income for the taxable year.

ART. 563. *Sale of capital stock, bonds, and capital assets.*— * * * If it sells its bonds at a discount, the amount of such discount is treated in the same way as interest paid, and if it retires its bonds at a price in excess of the issuing price, such excess may usually be deducted as expense. See articles 545 and 848 * * *

FILE COPY

IN THE

SUPREME COURT

OF THE

UNITED STATES.

October Term, 1935.

No. 525.

Great Western Power Company of California,

Petitioner,

vs.

Commissioner of Internal Revenue,

Respondent.

ON WRIT OF CERTIORARI TO THE CIRCUIT COURT OF APPEALS, SECOND CIRCUIT.

BRIEF FOR PETITIONER.

THOMAS R. DEMPSEY,
A. CALDER MACKAY,
1104 Pacific Mutual Building,
Los Angeles, California,
Attorneys for Petitioner.

Parker, Stone & Baird Co., Law Printers, Los Angeles.

TOPICAL INDEX.

PAGE

I.

Opinions 3

II.

Statement of the Case 4

(1) History of Case 4

(2) Facts 5

III.

Specification of Errors Relied Upon 9

IV.

Question Involved 10

Is the petitioner in the determination of its net taxable income for the year 1924 entitled to take as a deduction on account of the retirement of its bonds the unamortized discount and expenses of issuing said bonds and expenses and premiums paid in the retirement thereof? 10

V.

Argument 10

Article 545 of Regulations 65 specifically allows the deduction claimed by the petitioner 10

Conclusion 15

Appendix 1

TABLE OF AUTHORITIES CITED.

	PAGE
Brewster v. Gage, 280 U. S. 327	10
Commissioner of Internal Revenue v. Coastwise Transportation Co., 62 Fed. (2) 332, 71 Fed. (2d) 104	12
Fawcus Machine Co. v. United States, 282 U. S. 375	10
Helvering v. American Chicle Co., 291 U. S. 426	11
Helvering v. California Oregon Power Co., 75 Fed. (2) 644	11
Helvering v. Central States Electric Corp., 76 Fed. (2) 1011	11
Helvering v. Union Pacific R. R. Co., 79 L. E. Adv. Op. 145	11
Helvering v. Union Public Service Co., 75 Fed. (2) 723	11
Kohl v. United States, 91 U. S. 367	12
McCaughn v. Hershey Chocolate Co., 283 U. S. 488	11
Murphy Oil Co. v. Burnet, 287 U. S. 299	11
National Lead Company v. United States, 252 U. S. 140	10
San Joaquin Light & Power Corporation v. John P. McLaughlin, Collector of Internal Revenue, 65 F. (2d) 677	9, 11, 13
United States v. Kirby Lumber Co., 284 U. S. 1	11
Universal Battery Co. v. United States, 281 U. S. 580	10

T. D. 4603, XIV C. B. 46, p. 3	12
Treasury Regulations 65, promulgated under the Revenue Act of 1924, Art. 545	Appendix 1
Treasury Requisitions 65, Art. 545	14
Treasury Requisitions 45, Art. 544, in 1919	14

IN THE

SUPREME COURT

OF THE

UNITED STATES.

October Term, 1935.

No. 525.

Great Western Power Company of California,

Petitioner,

vs.

Commissioner of Internal Revenue,

Respondent.

ON WRIT OF CERTIORARI TO THE CIRCUIT COURT OF APPEALS, SECOND CIRCUIT.

BRIEF FOR PETITIONER.

I.

OPINIONS.

The opinion of the United States Board of Tax Appeals [R. p. 35] is reported in 30 B. T. A. 503. The opinion of the United States Circuit Court of Appeals, Second Circuit [R. p. 137], is reported in 79 Fed. (2d) 94.

II.

STATEMENT OF THE CASE.

(1) History of Case.

In determining the deficiency here involved for the year 1924, the respondent denied to the petitioner a deduction for unamortized discount and expense of issuance, premiums paid on retirement, and expense of retirement of those General Lien Convertible 8% Gold Bonds which were retired for cash, and also denied a similar deduction for like items in connection with the retirement of such bonds by the issuance of new bonds and the payment of a premium in cash. The petitioner appealed to the Board of Tax Appeals on these and other issues. On the hearing before the Board of Tax Appeals the respondent conceded the deduction with respect to the bonds retired by the payment of cash.

The Board of Tax Appeals held that both deductions were allowable and the respondent appealed to the Circuit Court of Appeals for the Second Circuit where he admitted the correctness of the Board's ruling with respect to discount and expense and premiums paid on the bonds retired for cash, but contended that no deduction was allowable with respect to the bonds retired by the issuance of new bonds. The said Circuit Court of Appeals agreed with the respondent and held:

> (1) That the deduction was allowable with respect to the unamortized discount and expense and premiums paid in the retirement of those bonds which were retired for cash at face value plus a 5% cash premium;

(2) That the deduction of such items was not allowable with respect to those bonds which were retired by the issuance of new bonds and the payment of a 5% cash premium; and

(3) That the unamortized discount and expense of issuance and premiums paid on retirement of the old bonds should be amortized over the term of the new bonds issued in exchange therefor.

In holding that the unamortized discount and expense and premiums paid on the old bonds retired were not deductible, the court held that the loss was not realized in 1924 and would not be realized until the new bonds issued in exchange therefor were to be retired.

(2) Facts.

On March 1, 1919, petitioner executed a trust indenture entitled "First and Refunding Mortgage" by which it conveyed all of its properties then owned and thereafter to be acquired to a corporate trustee as security for certain bonds to be thereafter issued pursuant to the terms of such indenture. Under this indenture petitioner issued four series of bonds entitled "First and Refunding Mortgage Sinking Fund Gold Bonds," the individual series being styled "Series A 6%," "Series B 7%," "Series C 6%" and "Series D 5½%," respectively [R. p. 66]. The only one of the above series material to the instant case is the "Series B 7%."

The "Series B 7% First and Refunding Sinking Fund Gold Bonds" (hereinafter referred to simply as the "Series B 7's") were dated August 1, 1920, and were due August 1, 1950. These bonds were issued during the year 1921,

the face amount of the issue being $8,500,000.00 [R. pp. 66. 80, 86, 87].

On February 1, 1921, petitioner executed another trust indenture entitled "General Lien Indenture" by which it conveyed all of its properties, subject to prior encumbrances, to another corporate trustee as security for another issue of bonds to be known as the General Lien Convertible 8% Gold Bonds (hereinafter referred to as the "General Lien 8's") [R. p. 99]. As further security for those who would become the holders of these General Lien 8's the indenture also provided that petitioner would, as promptly as possible under the laws of the State of California and the provision of the First and Refunding Mortgage, deposit and pledge with the trustee under the General Lien Indenture Series B 7's equal in par value to the General Lien 8's at any time issued and outstanding [R. p. 101].

During the year 1921 petitioner issued and sold to the public $2,500,000.00 face value of its General Lien 8's, the bonds being dated August 1, 1920, and due August 1, 1935 [R. p. 67]. During the same year petitioner issued and delivered to the General Lien trustees, as the additional security above referred to, a like amount of the Series B 7's [R. p. 69.]

The General Lien Indenture contained the following provision with regard to the redemption and conversion of the bonds issued thereunder:

"(Art. IV) REDEMPTION AND CONVERSION OF BONDS * * *

"SECTION 1. At any time when Series B bonds of the Company equal in par value to the par value of the bonds issued hereunder and then outstanding, shall be pledged and deposited with the Trustee hereunder, the Company may, at its option, redeem on any interest payment date, at the price of 105 together with accrued interest, all or any of the bonds issued hereunder and then outstanding; * * * [R. p. 101].

"SECTION 2. The holders of any and all bonds called for redemption shall have the option (to be exercised not later than the redemption date thereof) either of receiving payment for such bonds in cash at said price of 105 together with accrued interest, or of receiving for such bonds Series B bonds of the Company (with the coupon maturing on the interest payment date next following the redemption date and all subsequent coupons attached) equal in par value to the par value of the said bonds so called for redemption, and a premium in cash of five per cent. of the face value thereof and interest thereon to date of redemption. * * *" [R. p. 102.]

The General Lien 8's were issued (1921) at a discount of $150,000.00 and at an expense of $22,283.54 [R. p. 67]. Prior to December 31, 1923, petitioner had retired $11,000.00 face value of the General Lien 8's for cash and charged off in the year of retirement the then unamortized portion of the above discount and expense applicable to the bonds so retired [R. p. 67].

On May 8, 1924, $2,489,000.00 face value of the General Lien 8's were outstanding in the hands of the public, and on that date petitioner's Board of Directors passed a resolution calling all of such outstanding bonds for redemption on August 1, 1924, according to the terms of the General Lien Indenture [R. p. 67].

On August 1, 1924, the holders of $2,354,000.00 face value of the General Lien 8's exercised the option granted to them by the General Lien Indenture and exchanged their bonds for a like face amount of the Series B 7's. In addition to the Series B 7's received on this exchange each of the General Lien 8 holders received a cash premium equal to 5% of the face value of his General Lien 8's surrendered. The total premiums paid to the holders of the General Lien 8's so exchanged amounted to $117,725.00 and the expense of conversion was $1,461.05. The unamortized discount and expense of issuance applicable to the General Lien 8's so exchanged amounted, at the date of the exchange, to $126,176.97 [R. pp. 67-68.]

The $134,500.00 face value of the General Lien 8's which were not exchanged for Series B 7's were retired, by cash, as of August 1, 1924. A 5% cash premium was also paid to the holders of these bonds and the expense of retirement amounted to $83.46. The unamortized discount and expense applicable to these bonds at the time of retirement amounted to $7,207.82 [R. p. 68].

The respondent has conceded that the unamortized discount and expense of issuance, premiums paid, and ex-

pense of retirement applicable to the General Lien 8's which were retired for cash are allowable deductions for the year 1924 [R. p. 68], but contends that the same items applicable to the General Lien 8's exchanged for Series B 7's are not allowable deductions for 1924, but should be amortized over the lives of the Series B 7's. Petitioner agrees with the respondent with respect to the treatment of the items applicable to the General Lien 8's retired for cash, but contends that the same rule should be applied to the same items on the bonds exchanged.

III.

SPECIFICATION OF ERRORS RELIED UPON.

(1) The United States Circuit Court of Appeals for the Second Circuit erred in reversing the Board and in holding that the sum of $245,363.02 representing premiums, unamortized discount and expenses paid by petitioner in the retirement of $2,354,500.00 face amount of its General Lien 8% bonds was not deductible in the determination of petitioner's net taxable income for the year 1924.

(2) The United States Circuit Court of Appeals for the Second Circuit erred in reversing the decision of the United States Board of Tax Appeals.

(3) The United States Circuit Court of Appeals for the Second Circuit erred in failing to follow the decision of the United States Circuit Court of Appeals for the Ninth Circuit in the case of *San Joaquin Light & Power Corporation v. John P. McLaughlin, Collector of Internal Revenue,* 65 F. (2d) 677.

IV.

QUESTION INVOLVED

Is the Petitioner in the Determination of Its Net Taxable Income for the Year 1924 Entitled to Take as a Deduction on Account of the Retirement of Its Bonds the Unamortized Discount and Expenses of Issuing Said Bonds and Expenses and Premiums Paid in the Retirement Thereof?

V.

ARGUMENT.

Article 545 of Regulations 65 Specifically Allows the Deduction Claimed by the Petitioner.

Article 545 of Regulations 65 promulgated under the Revenue Act of 1924 provides that where bonds are issued by a corporation at a discount and later such bonds are purchased and retired, the excess of the purchase price over the face value minus any amount of discount deducted is a deductible *expense* for the taxable year of retirement.

This article has appeared without substantial change in each of the Regulations promulgated by the Commissioner under each of the Revenue Acts from 1918 to 1934, both inclusive, and since the article first appeared in its present form Congress has six times re-enacted the statute upon which it is based. The repeated reenactment of the statute in the face of this consistent administrative construction constitutes legislative approval of the statute so construed. (*National Lead Company v. United States,* 252 U. S. 140; *Brewster v. Gage,* 280 U. S. 327; *Universal Battery Co. v. United States,* 281 U. S. 580; *Fawcus Machine Co. v. United States,* 282 U. S. 375;

McCaughn v. Hershey Chocolate Co., 283 U. S. 488; *Murphy Oil Co. v. Burnet*, 287 U. S. 299.)

In addition to the legislative approval of this regulation this Honorable Court has expressly approved the article in the case of *United States v. Kirby Lumber Co.*, 284 U. S. 1, and has recently followed the doctrine of the *Kirby* case in *Helvering v. American Chicle Co.*, 291 U. S. 426.

Although Article 545 does not expressly cover the items other than discount and premiums, it has been held that the expense of issuing bonds is an additional cost of the capital secured and may be treated in the same manner as discount. (*Helvering v. Union Pacific R. R. Co.*, 79 L. E. Adv. Op. 145; *Helvering v. California Oregon Power Co.*, 75 Fed. (2) 644.) It has also been held that retirement expenses are deductible in the same manner as unamortized discount and expense of issuance. (*San Joaquin Light and Power Co. v. McLaughlin*, 65 Fed. (2) 677; *Helvering v. California Oregon Power Co.*, 75 Fed. (2) 644.)

Interpreting Artiele 545 in the light of the above cited cases, the courts have uniformly held that where an issue of bonds is retired for cash, *even though that cash be derived from the sale of a new issue of bonds*, the unamortized discount and expense applicable to the bonds retired, the premiums paid on retirement, and the expenses of retirement are all properly deductible in the year of retirement. (*Helvering v. California Oregon Power Co.*, 75 Fed. (2) 644, (C. A. of D. C.); *Helvering v. Central States Electric Corp.*, 76 Fed. (2) 1011 (C. C. A. 2); *Helvering v. Union Public Service Co.*, 75 Fed. (2) 723 (C. C. A. 8); *San Joaquin Light and Power Co. v. McLaughlin*, 65 Fed. (2) 677 (C. C. A. 9).

The Treasury Department also recognizes the propriety of such deductions in the case of bonds so retired. (T. D. 4603, XIV C. B. 46, p. 3.)

In view of this well settled construction of Article 545 the instant case seems to be resolved into a single question: Is there such a difference between bonds retired by cash secured from the sale of new bonds, and bonds retired by means of a direct exchange, as warrants the use of a different method of treating the items of unamortized discount and expense, premiums paid on retirement, and retirement expenses?

It is respectfully submitted that insofar as Article 545 is concerned, there is no difference whatever between these two types of retirement. The article simply states that if the bonds are "purchased and retired" the deduction is allowable; it does *not* limit the deduction to those cases in which the bonds are retired for *cash*. Moreover, we do not believe that any such limitation may be implied to the article. In neither its technical nor common meaning does the word "purchase" imply solely the use of money. Technically the word purchase includes all modes of acquisition other than that of descent (*Kohl v. United States,* 91 U. S. 367, 74); commonly it means to obtain anything by any outlay, as of labor, etc., or by paying money or its equivalent (Webster); and "generally, in statutes as in common use, the word is employed in a sense not technical, only as meaning acquisition by contract between the parties without governmental interference". (*Kohl v. United States,* 91 U. S. 367, 74.)

In this connection, it is interesting to note that in the case of *Commissioner of Internal Revenue v. Coastwise Transportation Co.,* 62 Fed. (2) 332; 71 Fed. (2d) 104,

the Circuit Court of Appeals for the First Circuit held that where a corporation retired its notes by exchanging its bonds therefor the transaction constituted a "purchase" of the notes within the meaning of Article 545 with a resultant taxable gain to the taxpayer. Clearly, we believe, if such an exchange was properly classed as a "purchase" for the purpose of fixing a taxable gain within the meaning of the Article, then a similar exchange must likewise be classed as a purchase for the purpose of fixing the amount of an allowable deduction within the meaning of the same Article.

We repeat, then, that insofar as the wording of Article 545 is concerned, there appears to be no reasonable ground of distinction between bonds retired for cash and bonds retired by an exchange of other bonds.

The theory advanced by the petitioner here is supported by the decision of the Board below and by the prevailing opinion in *San Joaquin v. McLaughlin,* 65 Fed. (2d) 677 (C. C. A. 9). On the other hand, the respondent's theory is supported by the decision of the court below and by the dissenting opinion in the *San Joaquin* case. Under the petitioner's theory the total amount of the unamortized discount and expense and premium paid upon the redemption of the General Lien 8's would be deductible in the year 1924 because the transaction was concluded in that year by the redemption of the old bonds and the extinguishment of the obligation. Under the respondent's theory, however, the obligation of the new bonds simply took the place of the obligation of the old and, therefore, no loss was realized in the year 1924. Under this theory the unamortized discount and expense and the premiums paid on account of the old bonds would be amortized over the life of the new issue.

We think that little can be accomplished by a discussion of the merits of these two theories. It seems sufficient to point out that at the time the respondent first issued his regulations on the subject of bond discount which, as we have seen, have received legislative approval, he undoubtedly knew of the different types of bond issues and also knew that frequently under various conditions old bonds are purchased and retired, *i. e.*, paid off, by the issuance of new bonds. Notwithstanding this he, nevertheless, promulgated his regulation and made no distinction therein between the bond "purchased and retired" for cash and the bond "purchased and retired" by the issuance of a new bond. That his regulation was a reasonable one is demonstrated by the fact, as heretofore shown, that it has received the approval of the courts and the Board of Tax Appeals. It is also reasonable from the standpoint of good accounting and conforms to accepted corporate accounting practices. Furthermore, it is reasonable from the standpoint of administration of the tax laws for the reason that it does not permit of pyramiding of bond discount and premiums from one issue to another; whereas it appears that if the opinion of the court below is to prevail, certain bond issues presently outstanding will have to carry annual amortization for, perhaps, several predecessor issues with the complications naturally attendant.

The Commissioner's regulation T. R. 65, Art. 545, was first promulgated at T. R. 45, Art. 544, in 1919. It seems significant that no case in which the present issue is involved came before the courts for more than ten years after the regulation was first promulgated; yet there were undoubtedly many cases in which the issue might have been raised.

Conclusion.

In conclusion, we submit that regardless of which of the two theories above mentioned one may adopt, he is, nevertheless, faced with the fact that the Treasury Regulations cover the point specifically and allow unamortized discount and expense and premiums paid upon retirement of bonds as deductions in the year in which such bonds are "purchased and retired"; that the particular regulation involved has the force and effect of law by reason of legislative approval; and that if the rule is to be changed it must be changed by Congress.

Respectfully submitted,

THOMAS R. DEMPSEY,
A. CALDER MACKAY,
1104 Pacific Mutual Building,
Los Angeles, California,
Attorneys for Petitioner.

APPENDIX.

Treasury Regulations 65, promulgated under the Revenue Act of 1924:

ART. 545. *Sale and retirement of corporate bonds.*—

* * * * * * * * *

(3) (a) If bonds are issued by a corporation at a discount, the net amount of such discount is deductible and should be prorated or amortized over the life of the bonds. (b) If thereafter the corporation purchases and retires any of such bonds at a price in excess of the issuing price plus any amount of discount already deducted, the excess of the purchase price over the issuing price plus any amount of discount already deducted (or over the face value minus any amount of discount not yet deducted) is a deductible expense for the taxable year. (c) If, however, the corporation purchases and retires any of such bonds at a price less than the issuing price plus any amount of discount already deducted, the excess of the issuing price plus any amount of discount already deducted (or the face value minus any amount of discount not yet deducted) over the purchase price is gain or income for the taxable year.

FILE COPY

FILED
NOV 5 193
CHARLES ELMORE CRO

No. 525

In the Supreme Court of the United States

OCTOBER TERM, 1935

GREAT WESTERN POWER COMPANY OF CALIFORNIA,
PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

MEMORANDUM FOR THE RESPONDENT

In the Supreme Court of the United States

OCTOBER TERM, 1935

No. 525

GREAT WESTERN POWER COMPANY OF CALIFORNIA, petitioner

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

MEMORANDUM FOR THE RESPONDENT

QUESTION PRESENTED

Where a corporation exchanges its B bonds and cash for its G bonds, under the terms of the G bonds, can it deduct the unamortized discount on the G bonds and the premium and expense incident to the exchange, in the year of such substitution, or must it amortize the same over the remaining life of its B bonds?

DISCUSSION

We do not oppose the granting of a writ of certiorari in this case. Petitioner, during the year 1921, pursuant to the provisions of its General Lien Indenture, issued and sold $2,500,000 face value of its General Lien 8 percent Gold Bonds dated February 1, 1921, and due February 1, 1936. These bonds, which will hereinafter be referred to as the "General Lien 8's," were sold at a discount of $150,000 and the expense of issuance was $22,283.54. The General Lien 8's were convertible under certain circumstances into Series B 7's (R. 64–65). Under the terms of the General Lien Indenture the holders of any and all General Lien 8's called for redemption had the option either of receiving payment in cash (5 percent above par) or of exchanging such bonds for Series B bonds of the company, par for par, and a 5 percent cash premium (R. 167–168).

The Series B 7's, dated August 1, 1920, and due August 1, 1950, were issued in the year 1921 (R. 66). Said Series B 7's were issued to a face value of $8,500,000 and were disposed of as follows: $2,500,000 delivered to the trustees under the General Lien Indenture and held by them as additional security for the General Lien 8's; $1,000,000 sold to the public in 1921 for cash at a discount of $100,000; and $5,000,000 delivered to trustees as additional security for another issue of bonds not here involved. The expense of issuing the entire Series B was $49,548.14 (R. 67).

On August 1, 1924, pursuant to a resolution adopted by the petitioner's board of directors on May 8, 1924, the holders of $2,354,500 face value of the General Lien 8's exchanged them for a like amount of Series B 7's and received, in addition to the Series B bonds, a cash premium. Such exchange was made in accordance with the provisions of the option granted by the General Lien Indenture (R. 112–113). The petitioner contends that the full amount of the premium, discount and expense incident to issue and exchange of these bonds is allowable as a deduction for the year 1924, whereas the Commissioner determined that such amount should be amortized over the life of the Series B 7's which were exchanged for the General Lien 8's (R. 66).

The premium, unamortized discount and expense of the balance of the General Lien 8's which were retired for cash have been conceded to be allowable deductions for the year 1924 (R. 66).

The court below held that the exchange of bonds was a mere substitution of the evidences of the same indebtedness, and, therefore, the petitioner had not realized the loss which it claimed (R. 223–227).

We submit that the court below applied the proper principles of law and reached a correct result. But in view of the fact that the decision of the Circuit Court of Appeals for the Ninth Circuit in *San Joaquin Light & Power Corp.* v. *McLaughlin*, 65 F. (2d) 677, is in direct conflict with

the decision of the court below, we do not oppose the petition.[1]

Respectfully submitted.

STANLEY REED,
Solicitor General.
FRANK J. WIDEMAN,
Assistant Attorney General.
JAMES W. MORRIS,
A. F. PRESCOTT,
Special Assistants to the Attorney General.

NOVEMBER 1935.

[1] It should be noted that the *San Joaquin* case involved both bonds retired for cash and bonds exchanged, while the question here is limited to the bonds exchanged.

U. S. GOVERNMENT PRINTING OFFICE: 1935

FILE COPY

FILED
FEB 18 19
CHARLES ELMORE

No. 525

In the Supreme Court of the United States

OCTOBER TERM, 1935

GREAT WESTERN POWER COMPANY OF CALIFORNIA,
PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT

INDEX

	Page
Opinions below	1
Jurisdiction	1
Question presented	2
Statutes and regulations involved	2
Statement	2
Summary of argument	6
Argument:	
The unamortized discount and expense applicable to bonds exchanged, pursuant to their provisions, for other bonds, together with the premium paid and expense of exchange, should be amortized over the life of the new bonds and not deducted in full in year of substitution	7
Conclusion	17
Appendix	18

CITATIONS

Cases:	
Aluminum Castings Co. v. *Routzahn*, 282 U. S. 92	9
Commissioner v. *Coastwise Transp. Corp.*, 62 F. (2d) 332, 71 F. (2d) 104	13
Helvering v. *California Oregon Power Co.*, 75 F. (2d) 644	12
Helvering v. *Central States Electric Corp.*, 76 F. (2d) 1011	12
Helvering v. *Union Pacific Co.*, 293 U. S. 282	8, 9, 10
Helvering v. *Union Public Service Co.*, 75 F. (2d) 723	12
Lucas v. *American Code Co.*, 280 U. S. 445	17
Niles Bement Pond Co. v. *United States*, 281 U. S. 357	9
Old Mission Co. v. *Helvering*, 293 U. S. 289	9
San Joaquin Light & Power Corp. v. *McLaughlin*, 65 F. (2d) 677	14
United States v. *Anderson*, 269 U. S. 422	9, 10
United States v. *Kirby Lumber Co.*, 284 U. S. 1	10
Weiss v. *Wiener*, 279 U. S. 333	16
Statute:	
Revenue Act of 1924, c. 234, 43 Stat. 253, sec. 234	18
Miscellaneous:	
47 Harvard Law Review, pp. 1260–1261	14
Treasury Regulations 65, art. 545	18

In the Supreme Court of the United States

OCTOBER TERM, 1935

No. 525

GREAT WESTERN POWER COMPANY OF CALIFORNIA, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT

OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 35–46) is reported in 30 B. T. A. 503. The opinion of the Circuit Court of Appeals (R. 137–142) is reported in 79 F. (2d) 94.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered July 29, 1935. (R. 142–143.) The petition for certiorari was filed October 17, 1935,

and was granted November 18, 1935. (R. 145.) The jurisdiction of this Court rests upon Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Where the petitioner in 1924 retired certain of its bonds, known as General Lien 8's, by exchanging therefor, pursuant to the provisions thereof, an equal amount of its Series B 7 bonds and paying the agreed cash premium, may the unamortized discount and issuance expense on the General Lien 8's, plus the premium and expense incident to the exchange or substitution, be deducted in full as a loss or expense of that year, or must the aggregate of such amounts be amortized over the remaining life of the Series B 7 bonds?

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set forth in the Appendix, *infra*, pp. 18–19.

STATEMENT

The facts were found by the Board of Tax Appeals (R. 36–43, 46–47), in accordance with the stipulation of the parties (R. 66–132). The facts material to the issue here presented may be stated briefly as follows:

Petitioner, a California public utility corporation, kept its books in accordance with the classification of accounts prescribed by the State Rail-

road Commission, to the jurisdiction of which it was subject, and filed its income tax returns on the accrual-basis. (R. 36–37, 66.)

On March 1, 1919, the petitioner executed a Refunding Mortgage on all property then owned and thereafter acquired, to secure the payment of bonds to be issued, as directed, from time to time in any number of series the directors might determine. It was provided that the bonds of any series might be redeemed or converted or exchanged for an equal face amount of bonds of another series, at the option of the holders, as should be determined by the directors. Under this indenture the petitioner issued four series of bonds known as Series A 6%, Series B 7%, Series C 6% and Series D 5½%, all which were duly authorized by the directors. (R. 37, 66, 74–94.)

On February 1, 1921, the petitioner executed a third trust indenture (the second, known as the Mortgage Indenture, not being material here), hereinafter called the General Lien Indenture (R. 99–107), pursuant to which there were issued and sold $2,500,000 face value of General Lien 8% Gold Bonds dated February 1, 1921, and due February 1, 1936. These bonds were sold at a discount of $150,000 and the expense of issuance was $22,283.54. (R. 37–38, 67.) The General Lien Indenture provided that the bonds issued thereunder should be secured by Series B bonds, in addition to other security, deposited from time to time with the trustee, that the petitioner might redeem the Gen-

eral Lien 8's at 105 plus accrued interest at any time Series B 7's, equal in face amount to the outstanding General Lien 8's, were pledged with the trustee, and that the holders of any General Lien 8's called for redemption had the right, at their option, to receive in exchange therefor Series B 7 bonds of equal par value plus a 5% premium in cash and accrued interest. This right of conversion into Series B 7 bonds was provided for in the General Lien 8 bonds issued. (R. 99, 101–102.)

During 1921 the petitioner, pursuant to resolutions of its directors (R. 80–87), issued under the Refunding Mortgage $8,500,000 par value Series B 7 bonds, dated August 1, 1920, and due August 1, 1950, at a total expense of $49,548.14. Of these bonds $5,000,000 were pledged as security for another bond issue not here involved, $2,500,000 were deposited and pledged with the trustee under the General Lien Indenture as security for the General Lien 8 bonds, and $1,000,000 were sold to the public for cash at a discount of $100,000. (R. 39, 68–69.)

Prior to December 31, 1923, the petitioner purchased and retired $11,000 face value of the General Lien 8 bonds and charged off as a loss of that year the unamortized discount and issuance expense applicable thereto. (R. 38, 67.)

On August 1, 1924, pursuant to a resolution of petitioner's directors, the holders of $2,354,500 par value General Lien 8 bonds exchanged the same, in accordance with the provisions of such bonds and of the General Lien Indenture, for a like amount

of Series B 7 bonds and in addition thereto a cash premium of $117,725. The unamortized discount and expense of issuance applicable to the converted bonds amounted on August 1, 1924, to $126,176.97, and the expense of conversion was $1,461.05. The unamortized discount and expense applicable to the General Lien 8's converted, the premiums thereon, and the expense of conversion aggregated $245,-363.02. The balance of General Lien 8's outstanding, face value $134,500, were purchased for cash and retired by the petitioner as of August 1, 1924, at an aggregate expense of $14,016.28, representing a premium of $6,725 plus unamortized discount and expense of $7,207.82 plus retirement expense of $83.46. (R. 38–39, 67–68.) All Series B 7 bonds not exchanged for General Lien 8 (or other) bonds were returned to the petitioner by the trustees of the several indentures with whom deposited and were not thereafter reissued. (R. 39, 40, 69.)

In addition to a deduction for unamortized discount and issuance expense, premiums and retirement expense on General Lien 8 bonds retired in 1924 for cash, which is admittedly allowable (R. 43–44), the petitioner claimed a deduction in 1924 for unamortized discount and issuance expense, premiums and retirement expense, aggregating $245,363.02, on the General Lien 8 bonds converted into or exchanged for Series B 7 bonds. This amount was not charged to profit and loss on petitioner's books, but was transferred to the Series B account to be amortized over the remaining life

of the Series B 7 bonds. The respondent denied the deduction of the latter amount in full in 1924, on the ground that it should be amortized over the life of the Series B 7 bonds substituted for the General Lien 8's, and allowed a deduction on account thereof in 1924 of $2,027.96. (R. 38, 43, 68, 74.)

The Board of Tax Appeals sustained the claim of the petitioner and allowed a deduction for 1924 of the full amount of unamortized discount and issuance expense, premiums and retirement expense on the General Lien 8 bonds exchanged for Series B 7 bonds. (R. 45–46.) The Circuit Court of Appeals reversed the decision of the Board and, sustaining the respondent, disallowed the deduction. (R. 142.)

SUMMARY OF ARGUMENT

Discount, premium and expense incident to an issue of bonds, and the retirement thereof, are all items of the cost of the use of the money. The amount of such items is not deductible in the year of issuance. The loss or expense represented by such cost is not sustained or incurred until the bonds are paid at maturity. Under the statute, however, as interpreted by the Treasury Regulations the cost may be amortized and a proportionate amount deducted annually during the life of the bonds. But the annual deduction of amortized discount, and other expenses, is allowed only by way of anticipation of actual payment of the bonds at maturity.

Here, the General Lien 8's in question were not paid at maturity, but prior to maturity they were exchanged for Series B 7 bonds of equal amount pursuant to the terms of the General Lien 8's. The old bonds were not paid and the indebtedness was not retired in the taxable year in question (1924). There was nothing more than a substitution of the Series B 7 bonds for the General Lien 8's, as provided for upon the issuance of the latter, and the debt remained, there being only a change in the paper evidence of the indebtedness. The money obtained from the original bonds was not repaid, but was retained by the taxpayer who continued to use it. Hence, the amount of the unamortized discount and expense, plus the premium and retirement expense, applicable to the exchanged bonds was not a sustained or realized loss or expense in the year of the exchange, but represented the cost of the use of the money for the period of the new bonds which must be amortized over the life of such bonds.

ARGUMENT

THE UNAMORTIZED DISCOUNT AND EXPENSE APPLICABLE TO BONDS EXCHANGED, PURSUANT TO THEIR PROVISIONS, FOR OTHER BONDS, TOGETHER WITH THE PREMIUM PAID AND EXPENSE OF EXCHANGE, SHOULD BE AMORTIZED OVER THE LIFE OF THE NEW BONDS AND NOT DEDUCTED IN FULL IN YEAR OF SUBSTITUTION

The petitioner seeks to deduct from its income in 1924 the full amount of the unamortized discount and expense of issuance, together with the premium and retirement expense paid, on its bonds con-

verted in that year, in accordance with their terms, into its bonds of another class. The Circuit Court of Appeals held that upon the substitution of the new bonds for the old there was only a change in the form of the obligation, the debt remaining to the extent of the face value of the substituted bonds, and that the petitioner received for the substituted bonds the net amount it had received for the old bonds less the expense of issuing the new and the additional expense of retiring the old. The unamortized discount and issuance expense of the old bonds, plus the premiums and retirement expense, represents the discount on and expense of issuing the new bonds and hence the aggregate of such amounts may not be deducted in full in the year of substitution, but must be amortized over the life of the new bonds and an aliquot part only deducted in each year. We submit that the decision below is correct.

Discount, premium, and expense incident to a bond issue are factors in arriving at the actual amount of interest paid for the use of the capital thereby procured. *Helvering* v. *Union Pacific Co.*, 293 U. S. 282, 286. A portion of each of the items is therefore attributable to each year of the life of the bonds, and that portion only is deductible each year.

There is no specific provision in the law which permits this amortization.[1] However, the statute,

[1] The regulations provide for the amortization of discount but make no specific reference to premium and expense. Article 545, Regulations 65, *infra* p. 18. See *Helvering* v. *Union Pacific Co.*, 293 U. S. 282, 284–285.

by authorizing returns on the accrual basis enables taxpayers to charge against the income of a taxable period expenses incurred in and properly attributable to the process of earning income during that period, even though payment is made in a later one. *United States* v. *Anderson,* 269 U. S. 422, 440; *Aluminum Castings Co.* v. *Routzahn,* 282 U. S. 92; *Niles Bement Pond Co.* v. *United States,* 281 U. S. 357. It is under this provision that expenses or obligations incurred in connection with a bond issue, which are not discharged until the payment of the bonds at maturity, may be properly amortized over the life of the bonds and allowed as annual deductions from gross income. *Helvering* v. *Union Pacific Co., supra.*

Amortized discount is deductible from the taxpayer's income only by way of anticipation of payment of the bonds at maturity. *Old Mission Co.* v. *Helvering,* 293 U. S. 289. It would seem to follow that amortized premium and expense are deductible only upon the same anticipation. As the Court stated in *Helvering* v. *Union Pacific Co., supra* (pp. 286–287):

> Both commissions and discount, as the Government concedes, are factors in arriving at the actual amount of interest paid for the use of capital procured by a bond issue. The difference between the capital realized by the issue and par value, which is to be paid at maturity, must be added to the aggregate coupon payments in order to arrive at the

> total interest paid. Both discount and commissions are included in this difference. If the difference be viewed as a loss resulting from the funding operation, it is one which is realized only upon the payment of the bonds at maturity.
>
> * * * * *
>
> They come out of the pocket of the taxpayer only on payment of the bonds at maturity.

But the bonds in the instant case were not paid at maturity. Before maturity petitioner merely substituted its new bonds to evidence the indebtedness. The exchange was made under the terms of the old bonds. The discoun had no more been paid after the issuance of the new bonds than it had been paid when the old bonds were issued. There remained the same obligation—a promise to pay—and the discount, premium and expense paid were properly chargeable to capital as representing a part of the cost of the use of capital during each year of the life of the new bond issue. Cf. *Helvering* v. *Union Pacific Co., supra;* cf. *United States* v. *Anderson, supra.*

No loss has been realized. Unlike the case of *United States* v. *Kirby Lumber Co.,* 284 U. S. 1, wherein the taxpayer actually purchased its bonds and on the net transaction had received more cash than it had paid for each bond, in the instant case the petitioner was still indebted to the holders of the old bonds (with whom the new bonds were exchanged) under and by virtue of the terms of the

old bonds, for the substitution of the new bonds for the old was a part of the original contract. After the issuance of the new bonds the same creditors remained, possessing no more than new evidences of the same debt. And the payment of the premiums pursuant to the terms of the trust instrument was just as much a discount attached to the Series B bonds as was the original discount attaching to the General Lien 8's.

The petitioner contends that the exchange "purchased and retired" the original bonds within the meaning of Article 545 of Regulations 65, *infra*, p. 18. Such a construction is not only contrary to that placed upon it by the Commissioner, but is opposed to the clear intent of the article—to treat premium, discount and expense as part of the cost of the use of capital (part of the actual interest paid) and to spread such cost ratably over the period of the indebtedness. In the instant case the Series B 7's were issued at the same time and as a part of the transaction pursuant to which the General Lien 8's were issued. The Series B 7's were placed in the hands of a trustee for the purpose of substitution for such of the General Lien 8's as to which the holders exercised their option to exchange. Clearly, there was no retirement of the original bonds within the meaning of the regulations. The debt evidenced by the old bonds was not paid and retired. The exchange merely effected a change in the paper evidence of the indebtedness

and did not terminate it in any sense. It therefore did not definitely fix the unamortized discount on August 1, 1924, as a part of the cost of the use of the money up to that date. The capital obtained by the issue of the old bonds was not returned at that time. The money, under and by virtue of the terms of the original contract, was to be, and was, used for a further period. The discount, premium, and expense are a part of the cost of its use for that further period. This fact was recognized by the State Railroad Commission as reflected by the books of the taxpayer, wherein the three items were transferred to "Discount and Expense Series B Account General Lien" to be amortized over the remaining life of the Series B 7's. (R. 66, 74.)

Helvering v. *Central States Electric Corp.*, 76 F. (2d) 1011 (C. C. A. 2d); *Helvering* v. *Union Public Service Co.*, 75 F. (2d) 723 (C. C. A. 8th); *Helvering* v. *California Oregon Power Co.*, 75 F. (2d) 644 (App. D. C.), are not opposed to the decision below and the views herein advanced. In each of those cases an outstanding bond issue was retired before maturity by payment in cash obtained from the separate sale of a new bond issue, which was unrelated to the earlier issue. In each case it was specially noted that there was no exchange or substitution of the new bonds for the old and that there was no interrelation or continuity of transactions, the retirement of the old bonds and the issuance of the new being wholly separate transactions. Ac-

cordingly, it was held that the unamortized discount and expense of the old issue, together with the premium and expense on retirement, were a deductible expense or loss in the year of retirement under the regulations. In the instant case the retirement of the General Lien 8's and the issuance of the Series B 7's, here involved, were directly interrelated and were in substance one continuing transaction.[2] The Series B 7's were merely exchanged or substituted for the General Lien 8's in accordance with the terms and conditions under which the latter were issued. Accordingly, the retirement of the General Lien 8's by substitution of Series B 7's therefor was not a completion of the transaction initiated by the issuance of the General Lien 8's.

Nor is *Commissioner* v. *Coastwise Transp. Corp.*, 62 F. (2d) 332, 71 F. (2d) 104 (C. C. A. 1st), inconsistent with the contention here made. There it was held that, upon the retirement of notes, representing the purchase price of property, by the issuance of bonds in exchange therefor, the face amount of the notes in excess of the par value of the bonds was taxable income. The exchange was not pursuant to the terms under which the notes were issued, but was an unrelated voluntary agreement subsequently entered into, and by that sub-

[2] To the extent that the General Lien 8's were retired for cash it has been conceded that the unamortized discount and expense, the premium and retirement expense, applicable thereto are a deductible loss or expense in the year of retirement.

sequent independent transaction the taxpayer reduced its indebtedness so that the transaction initiated by issuance of the notes was then completed, resulting in the acquisition of property or capital which would cost it no more than the face value of the bonds. There was no like completion of the transaction here, through a subsequent unrelated deal, resulting in a decrease of indebtedness.

In *San Joaquin Light & Power Corp.* v. *McLaughlin,* 65 F. (2d) 677 (C. C. A. 9th), it was held that upon the retirement of bonds of one issue, in part by the payment of cash and in part by an exchange of bonds of another issue pursuant to the provisions of the earlier issue, the amount of unamortized discount and expense, plus the premium and retirement expense, applicable to the old bonds, those exchanged for new as well as those retired for cash, is a deductible expense or loss in the year of retirement. So far as that case holds that the discount, premium and expense applicable to the exchanged bonds were a deductible loss or expense in the year of the exchange it is directly contrary to the decision of the lower court in the present case, and, we submit, is erroneous.[3] The correct view regarding the exchanged bonds we think is expressed in that case by Judge Mack, dissenting (pp. 681–682):

> The situation, however, as to the C bonds is, in my judgment, entirely different.

[3] See comment in 47 Harvard Law Review, pages 1260–1261.

Those D bondholders who made the exchange exercised a right that had been created when the D bonds were issued. The C bonds were issued at the same time for the very purpose of being substituted if the holders should exercise their option. When the exchange was made in 1922, the indebtedness originally created and evidenced by the 1492 D bonds was in no sense paid; its form was merely changed by an extension of the maturity, a decrease in the interest rate, in form to 6 per cent.; in substance, however, to a somewhat higher rate represented by the $40 cash premium, and the $10 cash discount paid at the time.

In my judgment, neither the unamortized part nor the premium was any more a loss to the company for the year 1922 than was the $10 discount. As appellee contends, this unamortized portion was in 1922 just what it was in 1920—a prospective, but not a realized, loss. It would become an actual loss only if and when appellant actually paid off and retired the bonds at par. The substitution of the new bonds pursuant to the original contract is not, however, a payment of the debt; the debt remains. One document has merely been substituted for another as evidence of it.

I concur, too, fully, in appellee's argument that the payment of the $50 in 1922, pursuant to the terms under which the original indebtedness was created in 1920, is just as much a discount attaching to the C bond as the original $70 was a discount attaching to the D bond.

It must be remembered that the discount, premium, and expense incident to an issue of bonds represent the cost of the use of the money, which is paid upon the maturity and payment of the bonds. No loss or expense is suffered or incurred until the bonds are paid in an amount in excess of the net proceeds obtained from the issuance, and the annual deduction of proportionate amounts of such cost is allowed only by way of anticipation of the actual payment of the bonds. With a due regard for this established principle, it seems clear that when the bonds are not paid but are exchanged for other bonds of equal amount, which are substituted for the old bonds in accordance with their terms, the amount of the unamortized discount and expense, plus the premium and retirement expense, applicable to the exchanged bonds is not a sustained loss or incurred expense in the year of the exchange. It might well be that upon the final payment and retirement of the indebtedness a gain, rather than a loss, will be realized. The statute is concerned only with realized losses, as with realized gains. *Weiss* v. *Wiener,* 279 U. S. 333.

It may be added that the petitioner was required by the State Railroad Commission to keep its books on the basis upon which the Commissioner has made his determination. Much latitude for discretion is given the Commissioner charged with the duty of enforcing the Act. Even where his determination is not in accordance with the method of ac-

counting employed by the taxpayer, his interpretation of the statute and the practice adopted by him should not be interfered with unless clearly unlawful. *Lucas* v. *American Code Co.*, 280 U. S. 445. *A fortiori* the Commissioner's determination should not be disturbed when in accordance with the method upon which taxpayer was required to keep its books, unless it be most clearly in conflict with the law.

CONCLUSION

The decision of the court below is correct and should be affirmed.

Respectfully submitted.

STANLEY REED,
Solicitor General.
FRANK J. WIDEMAN,
Assistant Attorney General.
SEWALL KEY,
JOHN MACC. HUDSON,
Special Assistants to the Attorney General.

FEBRUARY 1936.

APPENDIX

STATUTE AND REGULATIONS INVOLVED

Revenue Act of 1924, c. 234, 43 Stat. 253:

> SEC. 234. (a) In computing the net income of a corporation subject to the tax imposed by section 230 there shall be allowed as deductions:
>
> (1) All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, * * *;
>
> (2) All interest paid or accrued within the taxable year on its indebtedness, * * *
>
> * * * * *
>
> (4) Losses sustained during the taxable year and not compensated for by insurance or otherwise. * * *.

Treasury Regulations 65:

> ART. 545. *Sale and retirement of corporate bonds.*—* * *
>
> (3) (*a*) If bonds are issued by a corporation at a discount, the net amount of such discount is deductible and should be prorated or amortized over the life of the bonds. (*b*) If thereafter the corporation purchases and retires any of such bonds at a price in excess of the issuing price plus any amount of discount already deducted, the excess of the purchase price over the issuing price plus any amount of discount already deducted (or over the face value minus any amount of discount not yet deducted) is a deductible expense for the taxable year. (*c*) If, how-

ever, the corporation purchases and retires any of such bonds at a price less than the issuing price plus any amount of discount already deducted, the excess of the issuing price plus any amount of discount already deducted (or of the face value minus any amount of discount not yet deducted) over the purchase price is gain or income for the taxable year.

U. S. GOVERNMENT PRINTING OFFICE: 1939

SUPREME COURT OF THE UNITED STATES.

No. 525.—October Term, 1935.

Great Western Power Company of California, Petitioner, *vs.* Commissioner of Internal Revenue.	On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

[March 16, 1936.]

Mr. Justice Roberts delivered the opinion of the Court.

The parties disagree as to petitioner's right to deduct from gross income for 1924 unamortized discount, premiums, and expenses paid and incurred in that year in connection with the retirement of certain bonds. The petitioner took the deduction in its income tax return. The respondent disallowed it and determined a deficiency. The petitioner appealed to the Board of Tax Appeals which held the deduction proper.[1] The Circuit Court of Appeals reversed the Board's decision in part.[2] We granted the writ to resolve a conflict.[3]

March 1, 1919, the company executed a mortgage securing four series of bonds, one of which was designated "Series B 7%". February 1, 1921, the company executed another mortgage, securing bonds known as "General Lien Convertible 8% Gold Bonds", and thereby covenanted to deposit and pledge with the trustee Series B 7's equal in par value to the General Lien 8's at any time outstanding. The indenture provided that when this should be accomplished the debtor should have the right to redeem the General 8's at 105 and accrued interest, the holders to have the option to receive cash or Series B bonds, of equal face value, plus five per cent in cash. The General Lien 8's were issued at a discount of $150,000 and an expense of $22,283.54. Prior to December 31, 1923, certain General Lien 8's had been redeemed for cash and the then unamortized discount and expense allocable to the bonds retired had been charged off in the year of retirement. May 8, 1924,

[1] 30 B. T. A. 503.
[2] 79 F. (2d) 94.
[3] *San Joaquin L. & P. Corp.* v. *McLaughlin, Collector*, 65 F. (2d) 677.

the company called the remaining outstanding General Lien 8's for redemption August 1, 1924. The holders of $2,354,000 face value exercised the option to exchange for Series B 7's at par and a cash premium of five per cent. The total premium paid to them was $117,725 and the expense of the conversion was $1,461.05. The unamortized discount and expense of issuance in respect of the General Lien 8's thus exchanged, at the date of exchange, was $126,176.97. For the remaining General Lien 8's, which were not exchanged for Series B 7's, cash was paid at the rate of 105% of par and the company incurred certain expenses in the transaction. The total of the premium, the expense, and the unamortized discount applicable to all of the bonds redeemed for cash or in exchange for Series B bonds was charged off in 1924 and taken as a deduction from income for that year. The company keeps its accounts on the accrual basis. The Commissioner disallowed the entire deduction, but before the Board he admitted the propriety of so much of it as applied to bonds redeemed for cash. He insisted, however, that as to those retired by exchange of the Series B 7's the discount, premium, and expense should be amortized over the life of the latter. The Board overruled his contention, but the Circuit Court of Appeals sustained it, holding that the items would not be deductible as realized losses until payment or redemption of the Series B bonds, and should be amortized in annual instalments during their term.

Section 234 (a) of the Revenue Act of 1924[4] directs that in computing the net income of a corporation subject to the tax there shall be allowed as deductions ordinary and necessary expenses paid or incurred during the taxable year in carrying on the business, interest paid or accrued within the year on indebtedness, and losses sustained during the year not compensated by insurance or otherwise. The Treasury promulgated a regulation under the Revenue Act of 1918 covering treatment of discounts and premiums, which, with immaterial changes, has remained in force under all the revenue acts and appears as Art. 545 of Regulations 65 applicable to the Revenue Act of 1924.[5]

---

[4] c. 234, 43 Stat. 253.

[5] "ART. 545. Sale and retirement of corporate bonds.— . . .

"(3) (a) If bonds are issued by a corporation at a discount, the net amount of such discount is deductible and should be prorated or amortized over the life of the bonds. (b) If thereafter the corporation purchases and

Although the article does not expressly cover the items in question other than discount and premiums paid at redemption, expense in connection with the issuance of the securities is deductible on the same theory as unamortized discount.[6] It has accordingly been held that where an issue of bonds is retired for cash, whether the cash be obtained by the sale of a new issue or not, the items in question are deductible in the year of retirement.[7]

The question then is whether, upon an exchange of one obligation for another which is to be retired, the transaction is to be viewed as if the retirement were accomplished by the payment of cash. If the retired bonds had not been called, the expense items incurred in connection with their issuance would properly be amortized over the remainder of their life. Here the petitioner substituted a new obligation for the old. The remaining unamortized expenses of issue of the original bonds and the expense of the exchange are both expenses attributable to the issuance of the new bonds and should be treated as a part of the cost of obtaining the loan. They should, accordingly, be amortized annually throughout the term of the bonds delivered in exchange for those retired.

The judgment of the Circuit Court of Appeals is affirmed.

Affirmed.

A true copy.

Test:

Clerk, Supreme Court, U. S.

---

retires any of such bonds at a price in excess of the issuing price plus any amount of discount already deducted, the excess of the purchase price over the issuing price plus any amount of discount already deducted (or over the face value minus any amount of discount not yet deducted) is a deductible expense for the taxable year. (c) If, however, the corporation purchases and retires any of such bonds at a price less than the issuing price plus any amount of discount already deducted, the excess of the issuing price plus any amount of discount already deducted (or of the face value minus any amount of discount not yet deducted) over the purchase price is gain or income for the taxable year."

[6] *Helvering* v. *Union Pac. R. R. Co.*, 293 U. S. 282; *Helvering* v. *Cal. Oregon Pr. Co.*, 75 F. (2d) 644.

[7] *Helvering* v. *Cal. Oregon Pr. Co., supra; Helvering* v. *Central States Elec. Corp.*, 76 F. (2d) 1011; *Helvering* v. *Union Pub. Serv. Co.*, 75 F. (2d) 723; T. D. 4603, XIV C. B. 46, p 3.